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TRANSITION TO A SINGLE CURRENCY SYSTEM

Note by the Secretariat

Provides information concerning recent actions and developments, as well as issues encountered, with respect to the introduction of a single currency system of assessment based on the euro.

Background

1. At its eighth session, the General Conference adopted, beginning with the fiscal period 2002-2003, a single currency system of assessment based on the euro for contributions to the regular budget (GC.8/Dec.16 of 3 December 1999). With that decision, the Conference also amended the concomitant Financial Regulations of UNIDO relating to the preparation of budgets, appropriation and assessment, collection of contributions and advances, and currency of accounts. Since a certain portion of UNIDO's expenditures would continue to be in United States dollars, the Conference authorized the Director-General to establish a reserve, not subject to the provisions of financial regulations 4.2(b) and 4.2(c), for the purpose of protecting the Organization from exchange rate fluctuations. The Conference also requested the Director-General to report to its tenth regular session on the implementation of the transition to the single currency system.

2. To ensure a realistic comparison between the programme and budgets for 2000-2001 and those for future bienniums, a conversion of both the dollar and schilling components of the current budgets into euros was necessary (PBC.16/3). To facilitate such a conversion prior to the preparation of the budget proposals for 2002-2003, the Programme and Budget Committee approved an exchange rate for the 18 per cent of Member States' contributions which until 2001 were assessed in United States dollars (PBC conclusion 2000/4). The rate to be used was the average of the United Nations euro/dollar exchange rate for the period January to December 2000 (€1 = $0.925754), as reported in the proposed programme and budgets, 2002-2003 (IDB.24/3).

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3. At its ninth session the General Conference approved the exchange rate to be applied for the conversion into euros of assets, liabilities, reserves and fund balances as of 31 December 2001 (GC.9/Dec.15). In the same decision, the Conference noted that the Director-General would continue to keep extrabudgetary accounts in United States dollars, if required, but would convert all such assets, liabilities, reserves and fund balances for the purpose of the financial statements at the United Nations euro/dollar exchange rate in effect on the date of the statement (GC.9/Dec.15).

I. ACTION TAKEN TO INTRODUCE THE EURO

4. The Secretariat has kept the governing bodies regularly informed of the steps taken to introduce the euro (see list below). A conference room paper highlighting various actions and developments, as well as providing advance information on issues encountered was distributed at the twenty-fifth session of the Industrial Development Board (IDB.25/CRP.3, dated 26 April 2002).

5. **Preparation of the programme and budgets for 2002-2003**: The programme and budgets for the biennium 2002-2003 was prepared in euros. The 18 per cent dollar amount from the 2000-2001 regular budget (about $24.0 million) was converted to euros at the exchange rate approved in 2000 (i.e. €1 = $0.925754). The dollar requirements for 2002-2003 were also calculated at that exchange rate. The approved regular budget for the biennium 2002-2003 amounts to €133,689,800.

6. **New financial system**: A new financial system was developed and implemented within the shortest possible time to handle the dual currency requirements (i.e. the euro for the regular budget and United States dollars for technical cooperation activities financed from extrabudgetary resources) with effect from 1 January 2002.

7. **Financial regulations**: In compliance with decision GC.8/Dec.16 (b), the concomitant financial regulations were amended (Article III: regulation 3.2; Article V: regulation 5.1(d); regulations 5.5(d) and (e); Article X: regulation 10.5). An updated version of the Financial Regulations of UNIDO was issued as a separate conference room paper to the Board at its twenty-fifth session (IDB.25/CRP.4 of 23 April 2002).

8. **Conversion of assets, liabilities, fund balances and reserves**: All accounts, except for those relating to the extrabudgetary resources, were converted to euros effective January 2002 at the December 2001 United Nations rate of exchange (i.e. $1.0 = €1.123).

9. **Member States' obligations to the Organization**: All outstanding assessed contributions and advances to the Working Capital Fund were converted to euros at the same rate of exchange ($1.0 = €1.123), and Member States were informed of their new euro obligations.

10. **Issuance of allotments**: Programme managers have been given regular and operational budget allotments in euros. Furthermore, the allotment for the Regular Programme for Technical Cooperation has been issued in euros only.

Documents issued on the single currency system based on the euro, 1999-2001

Date	*Title*	*Symbol*
15 June 1999	Implications of the euro for UNIDO	IDB.21/29-PBC.15/15
31 August 1999	Implications of the euro for UNIDO	GC.8/15-IDB.21/30
18 November 1999	Implications of the euro for UNIDO. Intersessional working group on proposed amendments to the financial regulations	GC.8/19-IDB.21/31
11 July 2000	Conversion of the 2000-2001 programme and budgets into euros for comparison purposes	PBC.16/3
18 October 2000	Transition to a single currency system. Consultations with Member States on the definition of major objects of expenditure	IDB.23/15
1 November 2000	Transition to a single currency system. Consultations with Member States on the definition of major objects of expenditure	IDB.23/15/Add.1
23 March 2001	Introduction of the euro	IDB.24/10-PBC.17/10

11. **Establishment of a reserve**: As authorized by the General Conference (GC.8/Dec.16 (d)), a reserve has been established to protect the Organization from exchange rate fluctuations, i.e. to cover exchange gains and losses resulting from purchasing UNIDO's dollar requirements. However, at the beginning of the current biennium the reserve had a zero balance.

12. **Action taken to reduce dollar requirements**: The following payments relating to the regular and operational budgets are being made in euros to reduce the Organization's dollar requirements:

- Payments to consultants and experts;
- Payments to suppliers and contractors;
- Travel advances and settlements, with a few exceptions;
- All staff entitlements which are not promulgated in United States dollars. These include, inter alia, home leave, education grant (except for staff whose eligible children are outside the euro zone), language allowance, assignment and repatriation grants;
- Payments to the other Vienna-based organizations for various joint and common services;
- Payments to Van Breda and other health insurance schemes, except for those settled by the United Nations, New York.

II. ISSUES ENCOUNTERED

13. While the single currency system based on the currency in which most of the regular budget is implemented will allow more accurate accounting, expenditure planning, monitoring, reporting and simplification of the system of assessments, the implementation of the decision has a number of implications that have emerged since January 2002.

14. At the present stage, the Secretariat is not in a position to fully assess these implications, as a number of options are being explored, which will be discussed with the external audit team if necessary. A clearer picture is expected to emerge with experience and during the preparation of the accounts for the year 2002 and the biennium 2002-2003. Any issue requiring legislative approval will be brought to the attention of the governing bodies for decision. Some initial issues are outlined below.

Zero reserve balance

15. Although the General Conference authorized the establishment of a reserve for the purpose of protecting the Organization from exchange rate fluctuations arising from meeting dollar requirements (GC.8/Dec.16 (d)), the reserve had a zero opening balance. Moreover, the euro has depreciated against the United States dollar by about 4.3 per cent as compared to the rate approved by the General Conference for converting the dollar portion of the regular budget in the previous biennium (i.e. the conversion rate for the budget was €1 = $0.925754 while the average United Nations rate for the period January-June 2002 is €1 = $0.886001). In view of the zero balance in the reserve, an appropriate funding modality to cover the exchange losses needs to be explored. Furthermore, there is a need to specify and elaborate on the exchange losses that would be covered from this reserve.

Problems in reducing dollar requirements

16. During discussions by the governing bodies on the introduction of the euro and as reflected in various documents, it was recognized that it would not be possible to completely eliminate the dollar requirements, which amounted to some 18 per cent of the expenditures in previous bienniums. As stated in paragraph 12 above, the Secretariat has been striving to reduce its dollar requirements. However, a number of problems, as listed below, are being encountered.

17. **Staff salaries**: As the salary scales of Professional and higher categories of staff are promulgated in United States dollars by the International Civil Service Commission (ICSC) for the United Nations common system, the Organization is obliged to pay dollars to staff wishing to receive all or part of their salaries in dollars. This aspect can only be addressed with the issuance of salary scales in euros, which requires a United Nations system-wide solution. UNIDO is presently exploring the implications of issuing employment contracts to new Professional and higher categories of staff in euros only. Such a solution, however, cannot be applied to staff already on board. In order to find a system-wide solution, UNIDO raised this issue at the Human Resource Directors Network, a subsidiary of the Chief Executives Board for Coordination (CEB), in its meeting held 3-5 April 2002 in Geneva and also at the fifty-fourth session of the ICSC (Rome, April-May 2002). The issue is also an agenda item on the High Level Committee on Management—Finance and Budget Directors Network. At present, UNIDO is the only organization that has moved to a 100 per cent euro system, and therefore there appears to be no urgency to find a system-wide solution. However, the issue is expected to gain more prominence once other organizations with headquarters in the euro zone move to such a system.

18. **Pension Fund**: Since pensionable remunerations are promulgated in United States dollars (both for Professional and General Service staff), contributions to the United Nations Joint Staff Pension Fund (UNJSPF) will continue to be determined in United States dollars.

Negotiations were carried out with UNJSPF to pay in euros, but there is no major benefit to UNIDO under the terms offered. The UNJSPF requires UNIDO to pay the euro amount earlier than the dollar payments, and requires that the euro amount be determined using the applicable monthly United Nations rate of exchange.

19. **Field offices**: UNIDO Representatives and staff serving outside the euro zone (including in New York and Geneva) are expected to continue to receive salaries and other entitlements in United States dollars. Furthermore, operating costs of these offices, such as rent, maintenance, security and travel, will continue to be in dollars.

20. **Other United Nations organizations**: Payments to other United Nations organizations continue to be in United States dollars. These include, inter alia, payments relating to the Joint Inspection Unit, International Labour Organization Tribunal, United Nations (including the $1 million annual loan repayment), United Nations Office at Geneva, and the United Nations Development Programme.

Exchange gains and losses

21. In accordance with the General Conference decision, all regular and operational budget accounts were converted to euros on 1 January 2002 at the December 2001 United Nations rate of exchange. This included unliquidated obligations as of December 2001. As the euro has depreciated, exchange losses are experienced when payments are made against these obligations, although there is no change in the original dollar amount of obligation. A solution has been found, which has been endorsed by the External Auditor, under which such losses and gains, if any, would be charged to the prior biennium.

Management of extrabudgetary resources

22. Most extrabudgetary technical cooperation activities continue in United States dollars, but this is expected to change gradually with a shift in donor profiles. However, activities funded from within the euro zone are required to be carried out in euros. Furthermore, contracts, procurement, travel, engagement of consultants, etc. from within the euro zone are expected to be in euros, although the projects are dollar-based. This means that the entire project cycle management (such as the issuance of project allotment documents, disbursement, accounting, monitoring and reporting) for technical cooperation activities would have to be simultaneously in United States dollars and euros. The challenge, inter alia, is how to achieve this while minimizing exchange rate gains and losses (book or real) both to donors and to the Organization.

23. The next release of the financial software used by UNIDO, which is expected to be implemented later in the current year, would allow UNIDO to manage projects in both United States dollars and euros. However, this would not address the issue of exchange rate gains or losses. Therefore, various solutions are being explored by the Secretariat to be discussed with the External Auditor in due course, and the governing bodies will be informed of the outcome.

III. ACTION REQUIRED OF THE COMMITTEE

24. The Committee may wish to consider recommending to the Board the adoption of the following draft decision:

"The Industrial Development Board:

"(a) Takes note of the information provided in document IDB.26/4-PBC.18/5 on the transition to a single currency system, and in particular the problems being faced;

"(b) Notes with satisfaction that the Director-General is taking the necessary steps to ensure the implementation of the single currency system based on the euro;

"(c) Requests the Director-General to keep Member States regularly informed of further developments."