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**AGENDA ITEM 10.2:**  
**Sustainable Financing**

**Purpose of Paper**

1. To provide an update on actions undertaken by SPREP to date to address core budget pressures and thus ensure long-term sustainable financing for SPREP.
  - Audited Financials for 2018 continue to show favourable financial results for SPREP with continued surpluses in Financial Performance (3 years in a row since 2016) and more importantly, negative reserves accumulated since 2002 now removed based on a negative balance in 2016 of (\$443,762), \$5,123 balance in 2017 and now increased to \$139,740 by the end of 2018.
  - Despite the great improvement in the past 3 years, the challenge still remains for the Secretariat to maintain the positive performance and thus sustainability of funding with a view to rebuilding reserve funds and avoiding any further deficient positions in the future to ensure a strong financial position for the Secretariat moving forward.
  - This is more prevalent given the increasing portfolio for the Secretariat which doubled in size as per the 2018/2019 biennial budget of over US\$33 million compared to US\$15 million in 2017.

**Update**

**Policies**

2. The Secretariat completed and approved many of its policies on Financial Procedures including Procurement, Foreign exchange and Cost recovery in 2016 with the Reserves Policy that was remaining, completed and approved in December 2017. Hence all revised policies became effective from January 2017 while for the Reserves Policy since January 2018. Policies provide guidance but are not rigid, providing flexibility to allow for further review and consideration as and when appropriate.
3. The effectiveness of these policies is evident in the positive outcomes of the various audits and verification engagements (via the main SPREP annual audit and the various project audits and verification procedures) undertaken in the past year.

**Membership Contributions**

4. The Secretariat continues to engage and remind Members about the significant role that Membership Contributions play in relation to its composition of the budget. That is, it makes up about 3% of the 2019 Budget whilst 25% of the CORE Income.
5. Members contribution to the core are reflective of their ownership and commitment. There is considerable value-added of membership contributions in support of service delivery to Members' including significant leveraging impact that core funds can deliver in terms of tangible benefits for Members.
6. Outstanding payments on membership contributions was one of the contributing factors to the accumulated deficit and thus negative reserves over past years.<sup>i</sup>

7. Hence it is critical for Members to commit to payment of their annual contributions, including outstanding payments, as this prevents the reserves from running into a deficit/negative balance. If outstanding contributions are fully recovered, it will not only work against any deficits to the reserves but more importantly contributes to the rebuilding of the reserves funds again which is essential for covering for any unforeseen circumstances (e.g. liquidity shortfalls) in the future.
8. **Flexible payment plans** have been proposed by the Secretariat for outstanding contributions, and this has certainly assisted some Members to effectively pay its outstanding contributions over the years. For 2018, four Members were able to settle outstanding contributions carried from previous years with others continuing to make payments for reduction of carried forward balances. The Secretariat would encourage Members, especially those with significant outstanding membership payments, to use similar arrangements to address outstanding balances.
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10. **Regular reminders and follow up** notices continue to be sent out to members. A first notice in the first quarter has been circulated, with another follow up in June, and again in September. SPREP will continue to send out regular follow up notices every quarter to remind member countries of their commitment to pay membership fees, and to encourage payment of their contributions.
11. A proposal to **increase membership fees** was submitted at the 28SM in 2017 under various options to which a 20% increase was approved and supported in principle by the majority but subject to confirmation from Capitals/Governments.
12. Only Australia (20%), French Polynesia (10%), New Caledonia (20%), New Zealand (20%), Papua New Guinea (20%), Samoa (20%) and Tuvalu (20%) have responded to date (as at 18/6/19) to formalise pledges of approved contribution increases.
13. France and USA are not included in the agreement. (France's preference is for any contribution up to 20% which they have demonstrated by continuing to commit 5% additional contributions as in previous years. The USA is unable to commit beyond annual appropriations made by Congress

### **Programme Management Fees**

14. **Programme Management Charges** collected by the end of Dec 2018 totalled US\$1,059,865 which was a reduction by 14% compared to 2017 collections for Programme Management Charges. The result is evidence of some of the key projects seeing it to completion in 2018 as well as delayed implementation of many of the new donor projects envisaged in 2018 particularly for EU projects which were not signed until the last quarter of 2018 as well as delayed activities under the GCF VanKirap project.

15. The timeliness with respect to programme management charges and thus collection of these fees is largely dependent on the efficiency with which project activities are implemented as planned to which collaborative effort needs to be emphasised across all project teams in achieving.
16. **Timely and accurate monthly reports** on fees collected to date continue to be provided to Project Managers and Divisions to help them monitor and manage the collection of programme management fees.

### **Foreign Exchange**

17. Historically SPREP has been adversely impacted by the effects of foreign exchange losses, variable from year to year. Audited financial statements show that Forex losses amount to US\$265,351 in 2013, US\$200,789 in 2014 and in 2015 was US\$344,333. Since the effectiveness of the Foreign Exchange Policy and early implementation in in Sept 2016, we have managed to successfully control the Forex losses within a tolerable limit maxed at US\$100,000. Audited Financials for 2016, 2017 and 2018 notes Forex loss amounts of US\$98,000, US\$15,000 and US\$39,388 respectively.
18. The result is a significant improvement from past years' results and indicative of the continued effectiveness of measures undertaken by the Secretariat since 2016 to minimise the risk of foreign exchange exposure.
19. On-going measures undertaken by the Secretariat to combat the adverse impact of foreign exchange exposure include:
  - Close monitoring and regular revision of forecasted expenditure and income so that Foreign risk exposure can be minimised.
  - Minimising exposure risk by holding predominantly all accounts as well as contracts, funding agreements etc where possible in the reporting currency (USD).
  - Continued and regular discussions with Banks to address issues concerning foreign exchange exposure particularly with respect to negotiations as well as tools for managing foreign exchange transactions such as Forward Contracts, Terms of Foreign Currency Accounts etc.

### **Other Donor Fund Income/Other Income**

20. SPREP has been continuing discussions with non-traditional donors/partners for support
21. To date, Ireland has indicated its support for a core partnership arrangement of 3 to 4 years' worth up to US\$ 500,000. Additionally, potential partnership is currently explored with the World Bank and Norway.
22. In December last year, the government of China have formalised and indicated their commitment to an increase from USD\$150,000 to USD\$200,000 over the next 5 years and in addition to that, sponsorship of ten (10) Capacity Building programs/workshops for SPREP over this period.
23. SPREP in the current year is working on the development of a Donor Engagement/Partnership Framework Strategy with hopes to complete this year.

## Cost Control Measures

24. As evident from the results of the Audited Financials for 2018, the management team continues to effectively tighten up on cost control measures as part of its efforts to minimise costs in light of funding constraints over the past years. Evidently, total expenses for 2018 was noted at USD\$3.56 million compared to USD\$3.72 million in 2017.
25. Key areas of cost reduction are donations and sponsorships, personnel, SPREP Meeting costs, telephone and internet, and Other Expenses
26. With reference to the Audited Financials for 2018, overall cash expenditure (excluding depreciation of \$238,753 but including cash impairment of \$3,826) for Executive Management and Corporate Services was recorded at USD\$3.3 million compared to the 2018 budget of USD\$4 million. This was the result of continuous close cash flow monitoring and effective cash flow management particularly for Core Expenditure which saw the continuous reduction of monthly budget limits each month as an immediate measure to respond to noted gaps in income funding due to delays in key projects last year which had a significant impact on anticipated income.
27. Cost Recovery is reflective of good control over costs of which if based on the 2018 budget particularly for Operating Costs (\$1.495 mil), we only incurred expenditure for Executive Management and Corporate Support totalling \$762,627 for 2018. Cost savings totalling \$732,965 was derived not only from effective cost control measures implemented in light of evident funding constraints during the year, but also owing to effective cost recovery measures. Direct Cost Recoveries for Operating in 2018 was \$91,729.62 whilst noting a reduction as well in personnel costs for the Core as recoveries are seen as reductions in charges to the Core rather than actual income per se. (2018-\$2.45mil; 2017-\$2.54mil; circa \$90k reduction)
28. The 28SM held in Samoa in 2017 followed by the first Executive Board meeting thereafter, as was expected, resulted in a further cost reduction for the Secretariat given the significant costs involved for annual SPREP meetings in past years (US\$347k in 2014; US\$175k in 2015; \$220k in 2016; \$95k in 2017; \$44k in 2018). This is evidence of improved cost control and management over SPREP meeting costs and thus a positive impact of the decision by members to shift to Biennial SPREP meetings with Executive Board meetings in between instead of annual SPREP meetings.

## Recommendation

29. The Meeting is invited to:
  1. **consider** and **note** the above report on Sustainable Financing measures by the Secretariat.

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25 July, 2019

<sup>i</sup> For example, 2016 outstanding contributions (debit balance) was US\$556,981 yet the negative reserves as at 31/12/16 was US\$443,762. Had all the outstanding contributions been collected, reserves would not have been negative at \$443,762 but rather a positive balance of US\$113,219.