

INTERNATIONAL MONETARY FUND

The FY2008–FY2010 Medium-Term Administrative and Capital Budgets

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GLOSSARY

AFRITAC	African Technical Assistance Center
CBA	Cost-Benefit Analysis
CEP	Committee of Eminent Persons
CIO	Chief Information Officer
COB	Committee on the Budget
ECBR	Employment, Compensation, and Benefits Review
ESF	Exogenous Shocks Facility
FTE	Full-Time Equivalent (person year of employment)
HQ1	Headquarters Building 1
HQ2	Headquarters Building 2
IFRS	International Financial Reporting Standards
IT	Information Technology
KOA	Key Output Areas
LICs	Low Income Countries
MBP	Medical Benefits Plan
MTB	Medium-Term Budget
MTS	Medium-Term Strategy
PRGF	Poverty Reduction and Growth Facility
SRP	Staff Retirement Plan
TA	Technical Assistance

EXECUTIVE SUMMARY

- This paper presents proposals for the FY2008–FY2010 medium-term administrative budget (MTB) and the medium-term capital budget.
- The proposed MTB has been formulated against the background of work on sustainable financing for the Fund. While a new income model, building on the recommendations of the Committee of Eminent Persons (CEP), must play a major role in putting the Fund’s finances on a sustainable basis, expenditure restraint can and should also contribute to ameliorating the Fund’s finances over the medium term.
- This budget has, therefore, been formulated on the basis of seeking to deliver the MTS, as approved in April 2006, while cutting back the real administrative resources available to the Fund. The MTS envisages important changes in what the Fund does: additional resources are allocated to meet new needs and priorities of member countries, fully offset by raising the cost-effectiveness of existing operations and scaling back or eliminating lower priority activities. Thus, real cutbacks in the budget must be primarily achieved by increasing the efficiency with which the institution delivers a changing pattern of outputs.
- Accordingly, and as discussed at the February 2007 meeting of the Committee on the Budget (COB), the MTB envisages a 1 percent real reduction—measured against the external deflator—in the Fund’s net administrative expenditures (defined as gross expenditures less receipts) each year. As the Fund’s internal costs have tended to rise about 1 percent faster than the external deflator each year, the proposed MTB implies a reduction in the real administrative resources (staff numbers, travel volumes and level of support services) available to the Fund of about 2 percent each year. On this basis, by FY2010, the real administrative budget will have been cut by some 6 percent.
- The proposed MTB incorporates:
 - targeted reductions in input costs, particularly in support services, to achieve a relative shift from “back office” activities to “front line” work;
 - measures to ensure that Fund business practices and policies are in line with best practices of other International Financial Institutions, as appropriate; and
 - tighter budget constraints on, and enhanced monitoring of, all Fund departments and offices.
- While departmental business plans are still being finalized, the initial figures for FY2008 indicate there will be an increase in the share of administrative resources devoted to global monitoring. There will also be a small increase in the resources allocated to capacity building, with the Central AFRITAC coming fully into operation. Some further reduction in the share of resources devoted to Fund-supported financial programs and near program arrangements is anticipated. After allowing for certain classification changes, the share of resources devoted to country and regional surveillance is projected to remain broadly flat.

- At this juncture, the most significant further change in the pattern of outputs emerging for FY2009 and FY2010 is the increased share of resources going to country and regional surveillance, offset by a smaller share devoted to capacity building. (However, the latter is largely driven by conservative assumptions on the availability and application of external financing.) The small reduction in the share of resources going to global monitoring reflects the peaking of work on quotas and voice next year. Moreover, increasingly large planning reserves, not allocated to specific departments or outputs, are held in both years. These reserves are to allow not only, for example, for changes in the number of countries with Fund-supported programs, but also for the further implementation of MTS initiatives.
- The Executive Board is asked to appropriate \$922.3 million for FY2008 net administrative expenditures. This is an increase of 1.1 percent over last year's budget (1.7 percent on an underlying basis)—the lowest such increase in the last decade, and below the 2.7 percent increase in the Fund's external deflator. The Executive Board is asked to take note of the indicative budgets for FY2009 and FY2010, which rise by 1.7 percent and 2.3 percent, respectively.
- The Executive Board is also asked to approve an upper limit on gross expenditures of \$998.2 million, based on an upper estimate for receipts.
- Finally, approval is sought for \$46.6 million for capital projects beginning in FY2008. The Executive Board is asked to take note of the medium-term capital plan, totaling \$138 million; this represents a small nominal reduction in planned capital spending over the medium term relative to the FY2007 capital plan.

I. INTRODUCTION AND OVERVIEW

1. **This paper presents proposals for the FY2008–FY2010 medium-term budget (MTB) and seeks Board approval for the proposed FY2008 annual net administrative budget.**¹ The paper also presents the FY2008–FY2010 medium-term capital plan and seeks approval for expenditures on new capital projects beginning in FY2008. The impact of the proposed administrative and capital budgets on the Fund’s administrative expenses (as classified in the Fund’s financial statements), and hence on the Fund’s net income over the next three years, is identified.
2. **The income outlook assumed in this paper is consistent with that set out in the staff paper on the Fund’s income position.** As discussed in that paper, the outlook reflects the current policy stance on income and therefore does not incorporate possible options to develop a new income model.
3. **This paper is organized as follows.**
 - Section II describes the proposed top-down budget policy stance and the determination of the MTB envelope for FY2008–FY2010. This section identifies the specific measures proposed to reduce expenditures, relative to the estimated cost of current policies, and thus bridge the gap with the top-down budget policy constraint in FY2008. The areas where further reductions in costs will be sought to meet the indicative budget figures for the two outer years are also identified. The section also describes the MTB by planned output (the shares of administrative expenditures devoted to delivering each of the Fund’s Key Output Areas (KOAs) and constituent 12 outputs); and by input structure, in terms of the main categories of expenditure.
 - Section III presents projections on receipts and derives a proposed upper limit on gross administrative expenditures for FY2008, and indicative limits for FY2009 and FY2010.
 - Section IV presents the proposed medium-term capital plan and the FY2008 capital budget.
 - Section V indicates the estimated impact of the projected FY2007 administrative and capital expenditures on the Fund’s net income position.
 - Section VI concludes with the proposed decisions for Executive Board approval.

¹ From FY2007, the Executive Board approves the net administrative budget, based on a central estimate of receipts, and an upper limit on gross expenditures, based on a higher estimate of receipts. Accordingly, there is no gross administrative budget but rather a gross expenditure estimate.

II. THE PROPOSED FY2008–FY2010 MTB

A. The Budget Policy Stance

4. **At its meeting on February 22, 2007, the COB broadly endorsed management’s proposed budget policy stance for FY2008–FY2010.** The MTB envisages a 1 percent real reduction each year—measured against the external deflator—in the Fund’s net administrative budget. The Fund’s internal costs have tended to rise by about 1 percent more than the external deflator in recent years. Were this trend to continue, the proposed MTB would imply a reduction in real administrative resources (staff numbers, travel volumes and level of support services) of about 2 percent each year during the period. On this basis, the real budget would be cut by 6 percent by FY2010.
5. **The external deflator used to set the nominal budget is 2.7 percent, based on the formula agreed with the COB in December 2005.** Thus, the budget policy stance of a 1 percent real cut relative to the deflator implies a 1.7 percent nominal increase in the net administrative resources for each year of the MTB (as a standard assumption the external deflator is held constant over the medium term). However, the special addition made to the FY2007 budget for the costs of holding the Annual Meetings abroad must be excluded, before the FY2008 budget figure is calculated. Thus, the increase in the administrative budget proposed for FY2008, budget to budget, is 1.1 percent—the lowest rate of growth in the administrative budget in over a decade (Table 1 and Figure 1).
6. **At 2.7 percent, the external deflator is 0.3 percentage points lower than the estimate given in the paper presented at the February 2007 COB meeting; and it is 0.8 percentage points lower than the figure used last year in setting the FY2007–FY2009 MTB.** (The construction of the deflator and the figures for recent years are shown in Box 1.) This lower figure, relative to the assumption in the February 2007 COB paper, further reduces the size of the nominal net administrative budget proposed for FY2008 (and the indicative budgets for the two outer years). The figure now proposed for the FY2008 net administrative budget is \$2.7 million lower than that put forward to the COB in February, while the indicative net budget envelopes for FY2009 and for FY2010 are reduced by \$5.5 million and \$8.5 million respectively.
7. **This lower figure for the external deflator leads to a (slightly) greater squeeze on the Fund’s real administrative resources at least for next year.** If the lower deflator were to be translated into a fully corresponding lower increase in the Fund’s internal costs, then the effect would be neutral in real terms. In practice, the lower figure for the deflator will not be fully reflected in a smaller rise in the Fund’s internal costs. The main reason is that the increase in unit personnel costs, (and personnel costs account for more than 70 percent of gross administrative expenditures), is still estimated at around 4 percent in FY2008. Thus, staff estimate that, at most, the lower deflator will moderate the rise in internal costs by about \$0.8 million.

Table 1. Administrative Budget and Outturn Expenditures, FY1998–FY2008
(In millions of U.S. dollars, unless otherwise indicated)

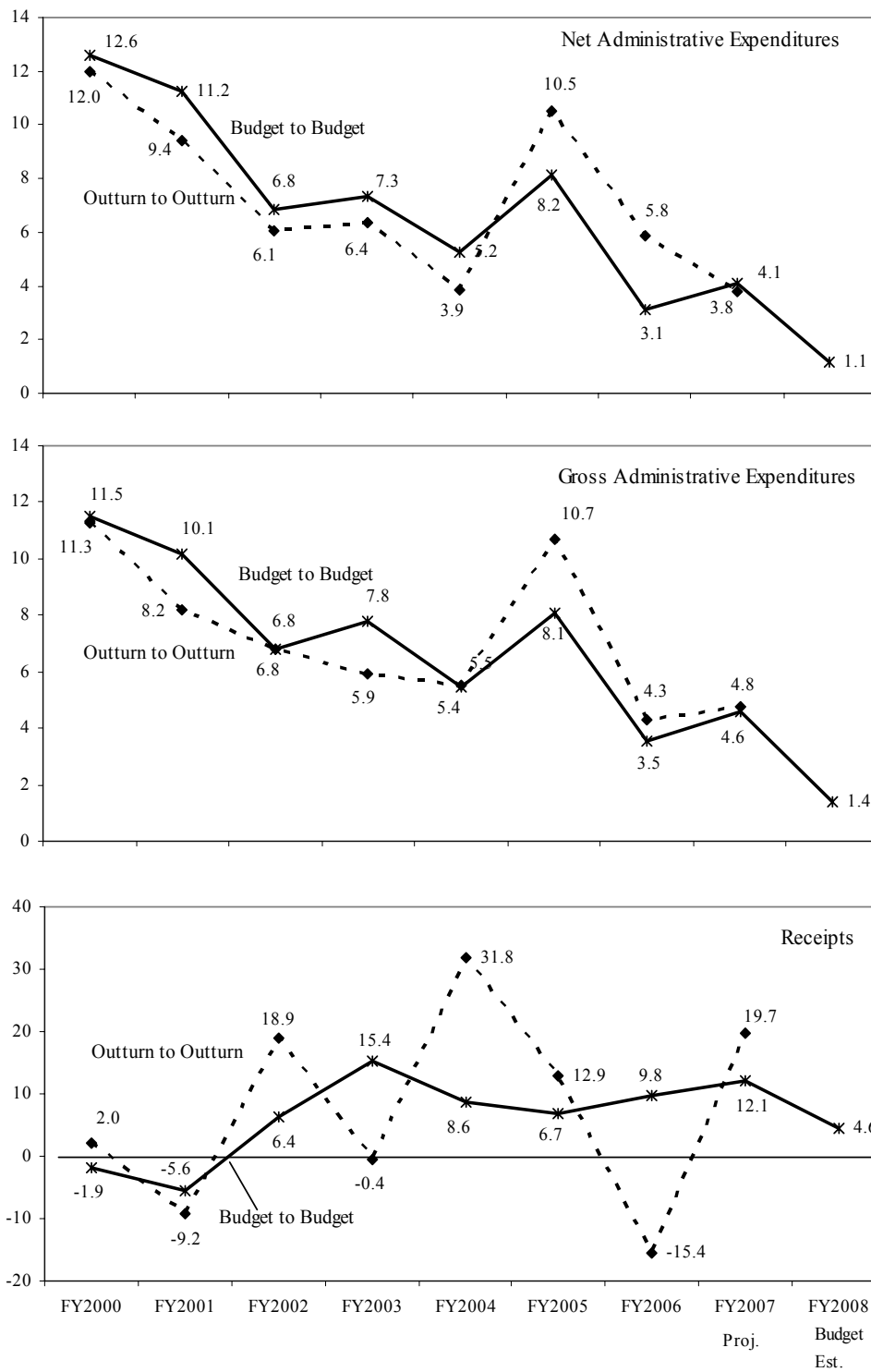
Financial Year	Budget	Outturn	Outturn to Budget Variance		Budget to Budget Increase		Outturn to Outturn Increase	
			Amount	Percent	Amount	Percent	Amount	Percent
A. Net Budget								
1998	503.7	495.3	-8.4	-1.7	13.2	2.7	23.8	5.0
1999	519.6	520.6	1.0	0.2	15.9	3.2	25.3	5.1
2000	585.1	583.0	-2.1	-0.4	65.5	12.6	62.4	12.0
2001	650.9	638.0	-12.9	-2.0	65.8	11.2	55.0	9.4
2002	695.4	676.7	-18.7	-2.7	44.5	6.8	38.7	6.1
2003	746.4	719.7	-26.7	-3.6	51.0	7.3	43.0	6.4
2004	785.5	747.6	-37.9	-4.8	39.1	5.2	27.9	3.9
2005 1/	849.6	826.1	-23.5	-2.8	64.1	8.2	78.5	10.5
2006	876.1	874.4	-1.7	-0.2	26.5	3.1	48.3	5.8
2007	911.9	907.6	-4.3	-0.5	35.8	4.1	33.2	3.8
2008	922.3	...	...	...	10.4	1.1	...	...
B. Gross Expenditures								
1998	545.2	531.1	-14.1	-2.6	18.7	3.6	20.2	4.0
1999	561.7	561.1	-0.6	-0.1	16.5	3.0	30.0	5.6
2000	626.4	624.3	-2.1	-0.3	64.7	11.5	63.2	11.3
2001	689.9	675.5	-14.4	-2.1	63.5	10.1	51.2	8.2
2002	736.9	721.3	-15.6	-2.1	47.0	6.8	45.8	6.8
2003	794.3	764.1	-30.2	-3.8	57.4	7.8	42.8	5.9
2004	837.5	806.1	-31.4	-3.7	43.2	5.4	42.0	5.5
2005 1/	905.1	892.2	-12.9	-1.4	67.6	8.1	86.1	10.7
2006	937.0	930.3	-6.7	-0.7	31.9	3.5	38.1	4.3
2007	980.2	974.5	-5.7	-0.6	43.2	4.6	44.2	4.8
2008	993.8	...	...	...	13.6	1.4	...	...

Source: Office of Budget and Planning.

Note: Figures may not add to totals due to rounding.

1/ FY2005 budget and expenditures include a \$48 million step increase in the Fund's contribution to the SRP.

Figure 1. Administrative Expenditures and Receipts: Rate of Growth, FY2000–FY2008 1/
(In percent)



Source: Office of Budget and Planning.

1/ FY2005 budget and expenditure figures include a \$48 million step increase in the Fund's contribution to the SRP.

8. **As a result, the cost of delivering the MTS on current policies in FY2008 is now estimated at \$20 million higher than the proposed budget envelope, vis-à-vis the \$18 million figure estimated in February.** In other words, actions to reduce administrative expenditures by some \$20 million must be taken to ensure consistency between the Fund's business and administrative policies and the proposed FY2008 budget. Further such action to close even larger gaps will be required for FY2009 and FY2010.

9. **The evolution of the proposed MTB envelope (both on a net and gross expenditure basis) is shown in Table 2.** This table reconciles the MTB figures now proposed, with the figures presented in February 2007, and the rolling forward of the FY2007–FY2009 MTB agreed by the Executive Board last year.

B. Allocating the Medium-Term Budget

10. **This year marks the implementation of a full medium-term administrative budget, with—for the first time—three-year business plans for Fund departments and offices.** As agreed in earlier discussions with the COB, the external deflator is held flat throughout the MTB period as a simplifying assumption, so that the budget figures for the outer years can reflect real changes—whether in output or input patterns or departmental allocations. But for the MTB to be meaningful, the figures must allow for uncertainty, not just on price and demand (volume) factors but also for the further implementation of the MTS itself, through the completion or downgrading of current exercises, and the emergence of new priorities and initiatives.

11. **Accordingly, the medium-term budget makes provision for centrally held reserves, that increase in size (as uncertainty increases) over the three-year period.** Thus, the first step in allocating the proposed medium-term budget was to make appropriate provision for centrally held reserves—that is, the contingency and central reserve for the forthcoming financial year, and planning reserves for the two outer years of the MTB.²

12. The FY2008 budget provides for a slightly larger contingency reserve than last year (\$4.6 million against \$3 million). This contingency reserve is now set at 0.5 percent of the net administrative budget and is designed to meet higher expenditures generated by exogenous demand or price (rather than policy) changes. Thus, these resources would be available, for example, to departments (on a demonstrated need basis) if the overall number of Fund programs were to increase, relative to plans, during the year. The reserve would also be available to accommodate any price changes, if for example the assumptions made about the rise in staff costs were overtaken by decisions still to be taken by the Executive Board at the time of preparing this paper.

² The reserves rise from 1 percent of the net budget in FY2008 to 1.6 percent in FY2009 and 2.2 percent in FY2010.

Box 1. The External Deflator

Following several discussions in the COB and the Executive Board in FY2006, Directors endorsed the use of an external deflator in setting nominal administrative budgets.

The agreed external deflator consists of:

- A personnel component, constructed as the weighted average of the most recent percentage changes in U.S. public sector salaries, financial sector total compensation, and private industrial sector total compensation; and
- A nonpersonnel component, set equal to the latest year-on-year change in the Washington-Baltimore Consumer Price Index.

The deflator is to be applied to all three years in setting the upcoming MTB envelope, and then updated each year in January, on a rolling basis. The deflator applied to the FY2007–FY2009 envelope was 3.5 percent; the deflator applied to the proposed FY2008–FY2010 envelope is 2.7 percent.

The External Deflator, FY1999-FY2008
(In percent per annum)

FY	Public Sector Compensation 1/	Private Financial Sector Compensation 2/	Private Industrial Sector Compensation 3/	Compensation Index 4/	Washington- Baltimore CPI 5/	External Deflator 6/
1999	2.5	6.5	2.2	4.0	0.6	3.0
2000	3.7	4.1	2.8	3.8	1.8	3.2
2001	4.9	5.8	3.7	5.2	2.5	4.4
2002	3.8	4.5	4.6	4.2	3.3	3.9
2003	4.8	4.2	4.0	4.5	1.8	3.7
2004	4.3	4.9	3.7	4.5	3.3	4.1
2005	4.4	7.5	4.3	5.6	2.2	4.6
2006	3.7	2.7	4.3	3.4	3.6	3.4
2007	3.4	2.7	4.6	3.3	4.1	3.5
2008	2.6	2.7	2.2	2.6	2.9	2.7

1/ Federal government scheduled salary increase for the locality pay area of Washington-Baltimore-Northern Virginia, as published by the U.S. Office of Personnel Management. For FY(X), percent increase effective January 1 CY(X-1) is used.

2/ Employment Cost Index for Total Compensation: Private Industry Workers: Service-providing industries: Financial Activities, excluding sales occupations; as published by the U.S. Bureau of Labor Statistics. For FY(X), percent increase in the index, Q4 CY(X-2) over Q4 CY(X-3), is used.

3/ Employment Cost Index for Total Compensation: Private Industry Workers: Goods-producing industries: White-collar Occupations, excluding sales occupations; as published by the U.S. Bureau of Labor Statistics. For FY(X), percent increase in the index, Q4 CY(X-2) over Q4 CY(X-3), is used.

4/ Calculated as: $0.5 \times \text{public sector percent change} + 0.4 \times \text{financial sector percent change} + 0.1 \times \text{private industrial sector percent change}$.

5/ Washington-Baltimore Consumer Price Index, as published by the U.S. Bureau of Labor Statistics. For FY(X), percent increase in the index, January CY(X-1) over January CY(X-2), is used.

6/ Calculated as: $0.7 \times \text{compensation index percent change} + 0.3 \times \text{Washington-Baltimore CPI percent change}$.

Table 2. Rolling Forward the Medium-Term Budget, FY2007–FY2010
(In millions of U.S. dollars)

	FY2007	FY2008	FY2009	FY2010
A. Approved FY2007–FY2009 MTB				
Net budget	911.9	929.6	952.8	
<i>percent increase on previous financial year</i>	4.1	1.9	2.5	
<i>excluding the additional cost of holding Annual Meetings overseas</i>	3.5	2.5	2.5	
Central receipts estimate	68.3	70.7	73.2	
Gross expenditures	980.2	1,000.3	1,026.0	
<i>Of which: Overseas Annual Meetings</i>	5.0	0.0	0.0	
B. Rolling forward the FY2007–FY2009 MTB to FY2008–FY2010				
Estimated net budget in February 2007		925.0	943.5	967.9
<i>percent increase on previous financial year</i>		1.4	2.0	2.6
<i>excluding the additional cost of holding Annual Meetings overseas</i>		2.0	2.0	2.0
Adjustment for revised deflator		-2.7	-5.5	-8.5
C. FY2008–FY2010 MTB				
Net budget		922.3	938.0	959.4
<i>percent increase on previous financial year</i>		1.1	1.7	2.3
<i>excluding the additional cost of holding Annual Meetings overseas</i>		1.7	1.7	1.7
Revised central receipts estimate		71.4	71.7	71.7
Gross expenditures		993.8	1,009.7	1,031.1
<i>Of which: Overseas Annual Meetings</i>		0.0	0.0	5.4
Upper receipts estimate 1/		75.9	76.1	76.2
Upper limit on gross expenditures		998.2	1,014.1	1,035.6

Source: Office of Budget and Planning.

Note: Figures may not add to totals due to rounding.

1/ Upper estimate based on the assumption that, with other receipts unchanged, those for capacity building are 10 percent higher than under the central estimate.

- The budget also sets aside a larger central reserve (\$5 million) vis-à-vis last year's \$3 million to accommodate MTS-related initiatives and other policy changes. A central reserve for MTS initiatives was introduced in FY2007. This approach was judged (and has proven to be) more effective in channeling resources to high priority work than releasing resources directly into departmental budgets, in anticipation of new developments that may not occur on time or in exactly the format or manner envisaged. For FY2008, this central reserve will be available to departments, again on a demonstrated need basis, for work to follow up on the recommendations of the Malan Committee, the CEP, further multilateral surveillance exercises and other MTS-related initiatives.
- For FY2009 and FY2010, sizeable planning reserves have been created. As noted, these larger reserves in the outer years will better enable the Fund to cope with the larger degree of uncertainty over time: the key objective is to ensure that resources are available to reflect new or changed modalities in the delivery of the MTS as it unfolds—as some current priorities intensify (or diminish as the work is completed)—within the overall agreed budget envelope. As the MTB is rolled forward, each year the resources in these planning reserves will be released to departments (with appropriate sums retained in the contingency and central reserve for the forthcoming budget year) in line both with the further evolution of MTS objectives and priorities, and emerging demand pressures.

13. **Within the MTB, the resources allocated to reserves and those available to be allocated directly to outputs (and hence departments and offices) are summarized in Table 3.** As noted in paragraph 8, the overall squeeze on the FY2008 budget implied by the top-down envelope relative to the estimated cost of continuing current policies is estimated at \$20 million. In terms of the resources available to allocate to outputs (and hence departments and offices), however, a further tightening is needed to make room for the \$3.6 million addition to reserves. Thus, in discussions with departments and offices, cost reducing measures totaling \$23.6 million had to be found for FY2008.

Table 3. Allocation of the Medium-Term Budget, FY2007-FY2010
(In millions of U.S. dollars)

	FY2007	FY2008	FY2009	FY2010
Gross expenditures estimate	980.2	993.8	1,009.7	1,031.1
Reserves	6.0	9.6	15.4	21.4
Contingency reserve 1/	3.0	4.6	n.a.	n.a.
Central reserve	3.0	5.0	n.a.	n.a.
Planning reserve	n.a.	n.a.	15.4	21.4
Gross expenditures allocated to outputs/departments (and offices)	974.2	984.1	994.3	1,009.7
<i>Of which: Overseas Annual Meetings</i>	5.0	0.0	0.0	5.4

Source: Office of Budget and Planning.

Note: Figures may not add to totals due to rounding.

1/ The formal contingency reserve is calculated as 0.5 percent of the net administrative budget. Note that the \$3 million held in central reserves in FY2007 was previously shown under building and other expenditures (see Table 5 below).

C. Cost Reducing Measures

14. **The proposed MTB thus incorporates a number of measures, described below, which aim to ensure that the MTS priorities and objectives can be fully delivered, despite the tighter real resource envelope.** The measures involve both targeted reductions in costs and a general squeeze on budgets to encourage greater efficiency, while delivering a changing pattern of outputs to member countries and the global community, in line with the MTS.

15. **First, a major element of the proposed MTB is to shift resources, in relative terms, from “back office,” primarily support activities, to “front line” work.** In this context, the MTB proposes the following measures.

- The ongoing examinations of support services, both the OIA zero-based review of support services and internal work within TGS, have identified considerable scope for cost reduction, mostly but not exclusively in non-staff costs—contractual services and procurement spending—while broadly maintaining current levels of service for next year. These measures will start to have an impact in FY2008, with enhanced cost reductions being achieved in the outer years.
- The first round of offshoring certain IT services that are already outsourced within the United States will also start reducing support service costs next year—again with greater savings being achieved in the two outer years.
- Some cost reductions will be secured from past and ongoing investments in IT projects—most of these will come from STA and TGS, with the rest from OBP. This is the return on past IT investments, with much of the savings arising from the lower numbers of clerical/administrative staff needed.
- In aggregate, some \$8 million in savings from support services will be secured next year with larger savings in the two outer years. The precise amounts in the two outer years, and any consequent changes in policies on support services, will need to be considered further in the light of the ongoing OIA reviews.

16. **Second, management is continuing to pursue specific efficiency and cost reducing initiatives, many of which are directed at ensuring that Fund administrative policies and practices are in line with best practices of comparable institutions.**

- The Travel Policy Working Group will be making recommendations for changes to policies and practices on official travel—airline ticketing, hotel booking, daily subsistence allowances (per diem), and other elements of official travel. The aim will be to bring the Fund’s policies more into line with standard business practices in other international financial institutions. For FY2008, some changes to the setting of per diem rates, (to cover meals and other expenses when staff are on official business) are envisaged. But the more substantive changes would involve changes to the way in which the Fund purchases air tickets and arranges business travel. The impact of any such changes will come mainly in FY2009 and beyond.

- Management has also commissioned a review of the Fund's separation policies and the financial provisions for such separations under the Separation Benefits Fund. For FY2008, the budget for the cost of staff separations will be set at \$5 million: thus with the expiration of the Staff Restructuring Initiative, which was introduced in FY2007 to finance staff separation costs arising from the MTS and the creation of MCM, the financial provision for staff separations will be reduced from \$9.7 million in FY2007 to \$5 million in FY2008.
- In aggregate the savings generated from these sources will be about \$6.5 million next year: but larger savings are expected in the two outer years, even before taking account of the further initiatives set out below.

17. **Looking forward to FY2009 and FY2010, with the ongoing program of cost reductions for support services already set in train, much of the focus will move to ensuring that administrative policies and practices are in line, as appropriate, with those in comparable international financial institutions.** Management has established a number of task forces and working groups, in addition to the Travel Policy Working Group, to review various aspects of such policies and programs. Their remits are summarized in Box 2. The objectives are to improve the design of these programs and ensure their long-run financial sustainability, as well as to temper the growth in their administrative costs. It is too early to assess potential savings arising from these reviews—and other reviews will likely also be undertaken (for example further zero-based reviews of departments).

18. **Third, all departmental and office budgets have now been agreed for FY2008: all groups—area departments, TA functional departments, other functional departments and support departments—face, to a varying extent, cuts in the real administrative resources available to them.** In line with modern budget practice, departments are given considerable flexibility on the application of their resources to different inputs. But, collectively, it is likely the number of staff years or Full-Time Equivalents (FTEs) will fall next year, as it has in each of the last two, as departments have to manage within increasingly tight budgets.

19. **The year-to-year changes in nominal departmental budgets in FY2008 vary both by broad category of department, and within each category from department to department, with much of the variation driven by MTS priorities and objectives.**

- On the one hand, the increase in nominal budgets for the area departments as a whole has been set only just below the levels needed to sustain their existing real resource base.³ On the other, for the support departments as a group, nominal budgets fall—the figures will be provided in the forthcoming companion paper.
- Within the non-TA functional category, FIN and RES will see their budgets grow in real terms as additional resources are allocated to them for work on quotas and voice and multilateral surveillance, respectively. By contrast, the OIA zero-based review of

³ This is after taking account of a technical adjustment made to devolve more responsibility for certain resident representatives expenses to area departments.

PDR, plus the further changes generated by the implementation of the MTS, will result in the nominal PDR budget remaining flat in FY2008, and a decline in FTEs.

- The introduction of performance measures next year will also enhance budget monitoring capacity, including the ability to undertake better review and comparative analysis of the delivery of departmental business plans.
- In aggregate, the downward pressure applied to departmental budgets in FY2008 will yield some \$9 million—exclusive of the further specific savings on support services identified above. For the outer years, as discussed below, it is intended that this general downward pressure on departmental budgets would remain firmly in place.

Box 2. Ongoing Management-Established Task Forces and Working Groups

- **The Task Force on the Reform of the MBP**, chaired by one of the Deputy Managing Directors, was established last year to address the relevant recommendations in the Employment, Compensation and Benefits Review (ECBR) and against the backdrop of the sizeable fluctuations from year to year in the financial health of the MBP. The task force is considering how to project and control medical costs more accurately, and how to slow their growth, while continuing to provide comprehensive coverage. The task force plans to complete its work during 2007 and to start implementing policy changes and some of the short-term administrative recommendations in FY2008.
- **The Travel Policy Working Group** established last summer is undertaking a comprehensive review of the Fund's travel policies, administration, and business model against best practices. The working group, which has largely completed its work, is focusing its key recommendations: on the scope to leverage the Fund's purchasing power in order to secure more favorable arrangements in purchasing airline tickets; and the need to ensure that the systems for the purchase of hotel accommodation, and the basis for setting the per diem allowances paid to staff traveling on Fund business, operate in a cost effective manner.
- **The Task Force on SRP Reform**, chaired by one of the Deputy Managing Directors, and established last May, is reviewing the Fund's retirement benefits to see how the present approach, which will continue to provide the defined benefit scheme, can also be adapted to meet evolving staffing requirements. In this context, the task force is examining the level and service-based rate of accrual of benefits consistent with the relevant standards of competitiveness, and will determine whether changes may be needed—such as complementing the current pension system with a voluntary savings plan, and other measures that could facilitate benefits portability for short-term and mid-career appointments. This work is expected to be completed by this fall. The task force will then review and evaluate a change in the SRP remuneration base and the payment of pensions, comparing the current gross with a net-of-tax salary basis that would be accompanied by a tax allowance payment for any income tax paid on pensions.

D. Delivering the Strategy within the MTB

20. **Within the MTB envelope, the allocation of resources proposed for FY2008 is designed to enable the full delivery of the objectives of the MTS.** The principal objectives of the MTS may be summarized as follows:

- **Modernizing the framework for surveillance and continuing to improve its effectiveness**, through sharper and more focused surveillance, greater emphasis on the financial sector, increased stress on external stability, better analysis of spillovers through stronger multilateral and regional surveillance, and the streamlining of Article IV reports;
- **An enhanced role in crisis prevention in emerging market economies**, through strengthening the Fund's ability to diagnose vulnerabilities, greater focus on financial and capital markets, the broadening of the Consultative Group on Exchange Rate Issues (CGER) to include major emerging market currencies and consideration of a new liquidity instrument (the Reserve Augmentation Line). The Fund is also strengthening its preparedness for crisis management;
- **More effective engagement in low-income countries (LICs)**, through new instruments (the Policy Support Instrument and the Exogenous Shock Facility), debt relief (Heavily Indebted Poor Countries and Multilateral Debt Relief Initiative), better policy advice and program design, a rigorous debt sustainability framework, clarifying the Fund's role in LICs as well as its interactions with donors, and improved coordination with the World Bank (Malan report);
- **A more integrated approach to capacity building**, through better alignment of capacity building efforts within the overall Fund and country priorities, an enhanced role for area departments in setting priorities and better targeting of activities; and a more effective engagement in LICs (e.g., by full operation of the new regional technical assistance center in Africa—Central AFRITAC);
- **Governance reforms**, with consideration of a new quota formula and increase in basic votes; and an increase in staffing resources for Executive Directors elected by a large number of members; and
- **Putting the institution on a more stable financial basis**, through development of a new income model following the CEP report, in parallel with the implementation of real spending cuts as part of MTB/MTS and further budget reforms—including the introduction of Fund-wide performance indicators.

21. **At this juncture, the information available on the planned changes to the Fund's pattern of outputs and activities over the next three years is preliminary, as departmental business plans have not yet been finalized.** The present activity indicators, which do not fully capture the changing pattern of Fund work, are being replaced by new performance indicators as from FY2008 (and the specific proposals will be described in the relevant companion paper). The information on the allocation of Fund administrative expenditures, that is the input of staff, travel and support service resources, to outputs, the 4 KOAs and 12 constituent outputs is rather better; but there are some important changes between the FY2007 and FY2008 figures. A review of the existing systems for allocating staff time and other resources, and the scope for better matching them to the emerging pattern of Fund outputs and the introduction of performance indicators, led to changes in the way certain resources are allocated to the various outputs (Box 3). In part, the differences emerging in the initial figures for FY2008 are driven by these reclassifications, but in part

they also reflect genuine shifts in the application of resources—making the FY2007 to FY2008 changes difficult to interpret.

22. **That said, the information available for FY2007 suggests a reallocation of staff and other resources in line with MTS objectives is already taking place; and the initial figures from departmental business plans indicate these changes will be taken further in FY2008.** Table 4 provides a breakdown of the FY2008 gross expenditures by KOAs and by the 12 constituent outputs as they are emerging in departments' draft business plans. The following main developments can be, at least provisionally, identified at this stage:

- **Within a declining real administrative resource envelope, the FY2008 budget reallocates resources from back office activities to work on KOAs.** In practice, this implies shifting dollar resources—in relative terms—from support departments to area and functional departments. (OED and IEO expenditures are assumed to increase broadly in line with the external deflator.)
- **An increase in the share of administrative resources going to global monitoring and within that KOA, particularly to oversight of the international monetary system is envisaged in the emerging departmental business plans.** In part, this shift is a result of a reclassification of staff time and other resources, but it also reflects a redeployment of resources for increased work on quotas and voice and on general outreach—a priority under the MTS. The downward trend in the outer years reflects an anticipated peaking of work on quotas and voice in the next financial year.
- **The share of resources devoted to capacity building in FY2008 is expected to be slightly higher than in FY2007, but is then projected to fall a little over FY2009 and FY2010.** The FY2008 planned share takes account of the full operation of the Central AFRITAC next year. Over the remainder of the MTB, the prospective small fall in the share of administrative resources devoted to capacity building principally reflects the expected decline (in real terms) in the drawdown of donor funds, in line with the central estimate of receipts discussed in the next section. If, however, there were both higher availability of external monies for technical assistance work, and the capacity within the relevant departments to marshal the necessary resources (largely the services of short-term experts), there could be an increase in the share of resources devoted to capacity building.
- **The figures for both the country specific and regional monitoring and country programs and financial support KOAs are more difficult to interpret, and are being further reviewed.** The year-on-year fall in the share of resources being allocated to each KOA in FY2008 is driven principally by a reclassification. As is to be expected, the figures for country programs and financial support remain broadly flat over the remainder of the MTB period—since, by assumption, the number of Fund-supported financial and near programs is held constant. The rise in the share of resources going to country specific and regional monitoring in part reflects increased further application of resources to financial sector work.

Box 3. Further Changes to the Allocation of Administrative Expenditures to Output

A recent review has led to further changes in the allocation of gross expenditures to outputs, following the recommendations of the Second Task Force on Performance Indicators, and taking account of the new patterns of output emerging in the FY2008 departmental budget submission.

The reclassifications include:

- (i) The task force determined that operational support to the Board of Governors and the IMFC is a final output of the Fund. Thus, it has been reclassified from Governance to Global Monitoring, in particular Oversight of the International Monetary System.
- (ii) The administrative costs incurred by INS for the management of the Institute training program were reallocated from technical assistance to external training.
- (iii) EXR has reclassified some of its support costs (mainly in the area of publications) into general outreach.
- (iv) The allocation of building and other expenses has been revised on the basis of departmental budget submissions.

Examples of departments redeploying resources to meet new MTS priorities (some of which began in FY2007) include:

- (i) EXR is putting more resources into general outreach and less into country work and general support activities.
- (ii) FIN is shifting resources into income and quota work.

Table 4. Estimated Gross Administrative Expenditures by Key Output Area
and Constituent Output, FY2007-FY2010 1/
(In percent share of total gross expenditures, excluding reserves)

	FY2007 2/ Estimated Outturn	FY2007 2/ Projected Outturn	FY2008 Budget	FY2009 Budget	FY2010 Budget
Global Monitoring	14.1	14.2	17.4	17.2	17.0
Oversight of the international monetary system	...	3.8	5.0	4.9	4.8
Multilateral surveillance	...	4.0	4.6	4.6	4.5
Cross-country statistical info. & methodologies	...	3.2	3.0	2.9	2.9
General research	...	0.1	0.4	0.4	0.4
General outreach	...	3.1	4.3	4.3	4.3
Country specific and regional monitoring	33.9	36.7	33.7	34.3	34.5
Bilateral surveillance	...	30.6	27.7	28.1	28.3
Regional surveillance	...	2.6	2.8	2.9	3.0
Standards and codes and financial sector assessments	...	3.6	3.2	3.2	3.3
Country programs and financial support	27.2	25.1	24.4	24.5	24.6
Generally available facilities	...	13.7	11.1	11.1	11.2
Facilities specific to low-income countries	...	11.4	13.3	13.4	13.5
Capacity Building	24.8	24.0	24.5	24.0	23.8
Technical assistance	...	20.0	17.4	16.9	16.8
External training	...	3.9	7.1	7.1	7.0
Total, excluding reserves	100.0	100.0	100.0	100.0	100.0
<i>Memorandum items (in millions of U.S. dollars):</i>					
Governance	96.1	92.6	90.6	93.2	97.5
Reserves 3/	3.0	n.a.	9.6	15.4	21.4
Total gross expenditures	980.2	955.5	993.8	1,009.7	1,031.1

Source: Office of Budget and Planning.

Note: Figures may not add to totals due to rounding.

1/ Because of the changes discussed in Box 3, the figures for FY2007 and FY2008 are not directly comparable.

2/ From FY2007, the Executive Board approves the net administrative budget, based on a central estimate of receipts, and an upper limit on gross expenditures, based on a higher estimate of receipts. Accordingly, there is no gross expenditure budget but rather a gross expenditure estimate.

3/ Includes the contingency and central reserves for FY2008; and the planning reserves for both FY2009 and FY2010.

23. **The indicative information for the two outer years of the MTB in Table 4 need to be interpreted with particular caution.** What is identified is the relative share of resources to be devoted to each output. In developing their business plans, departments faced a 3 percent real reduction in their budgets for FY2009 and FY2010. The combination of the overall budget policy stance—a 1 percent reduction against the external deflator and the assumed continued further 1 percent gap between the deflator and the rise in the Fund’s internal costs—plus the application of a 1 percent efficiency tax to create higher reserves, effectively squeezed departmental budgets by around 3 percent in each of the outer years. While in reality there will be some release of resources from the planning reserves to departmental budgets, as the MTB is rolled forward, the tight stance for the outer years is intended to challenge departments to scrutinize activities and raise efficiency. But the release of resources from the reserves will also likely lead to further changes in the planned share of resources going to the different outputs.

E. The Proposed MTB by Input

24. The proposed FY2008 administrative budget by main input category shows a further small shift in the allocation of resources from building and other expenses towards the personnel and travel categories (Table 5). This shift in part reflects the measures, described earlier, to reduce the costs of support services—many of which are recorded in the building and other expenses category. But the shift also reflects the impact of relative price changes, as a gap remains between the projected price increase for personnel and that for other expenditure items. Since staff are largely a fixed factor of production in the short term, departments have typically tried to absorb the increase in the staff’s unit costs (or standard costs, as described below) by reducing the other more variable production factors. The share of travel in gross expenditures is also budgeted to increase in FY2008, as departments have planned for higher outreach and TA-related travel (for example to the new AFRITAC).

25. **In FY2008, the Fund’s overall internal costs are estimated to grow by slightly less than 4 percent (budget to budget), some 2 percent more than the underlying increase in the net administrative budget envelope.** The main driver of the Fund’s internal cost structure is the projected increase in staff standard costs—essentially average staff salaries plus staff benefit payments. Box 4 describes the standard cost concept in more detail and how it is computed. Standard costs for staff are estimated to increase by about 4 percent in FY2008, relative to the FY2007 budget figure, while both travel costs and the cost index for the buildings and other expenses category are assumed to rise in line with the external deflator (by 2.7 percent).

26. **The projected rate of increase in the Fund’s standard costs for FY2008 is based on working assumptions about a number of decisions that the Executive Board will be asked to take by the end of the current financial year**—in particular, the 2007 staff compensation award and the annual budgetary contributions to the SRP; and the MBP. As at this stage last year, there is still some uncertainty on the outcome of the Board’s discussion, for example on the staff compensation award, and the final figures for the comparatio and recovery rate.

Table 5. Administrative Budget by Major Expenditure Category, FY2007—FY2010
(In millions of U.S. dollars, unless otherwise indicated)

	FY2007				FY2008		FY2009		FY2010	
	Budget	Percent Share 1/	Projected Outturn 2/	Percent Share 1/	Budget	Percent Share 1/	Budget	Percent Share 1/	Budget	Percent Share 1/
I. Personnel	700.2	71.9	712.1	73.1	723.1	73.5	735.5	74.0	748.0	74.1
Salaries	407.5	41.8	405.0	41.6	424.6	43.1	430.4	43.3	436.7	43.3
Benefits	292.7	30.0	307.1	31.5	298.5	30.3	305.1	30.7	311.3	30.8
II. Travel	97.0	10.0	91.6	9.4	100.5	10.2	100.4	10.1	98.1	9.7
III. Building and other expenditures	171.9	17.6	165.3	17.0	160.6	16.3	158.4	15.9	158.2	15.7
IV. Annual Meetings	5.0	0.5	5.4	0.6	0.0	0.0	0.0	0.0	5.4	0.5
V. Reserves 3/	6.0	0.6	0.0	0.0	9.6	1.0	15.4	1.5	21.4	2.1
Gross Expenditures	980.2	100.6	974.5	100.0	993.8	101.0	1,009.7	101.5	1,031.1	102.1
Receipts	-68.3	-7.0	-66.9	-6.9	-71.4	-7.3	-71.7	-7.2	-71.7	-7.1
Net Administrative Budget	911.9	93.6	907.6	93.1	922.3	93.7	938.0	94.3	959.4	95.0

Source: Office of Budget and Planning.

Note: Figures may not add to totals due to rounding.

1/ Percent of gross expenditures allocated to outputs (gross expenditures less reserves).

2/ Includes the additional contribution to the SRP Service Credit Program. Note that, excluding this additional contribution, the share of personnel in gross expenditures allocated to outputs is projected at 72.5 percent.

3/ Includes the contingency and central reserves in FY2008 and the planning reserves in FY2009 and FY2010. Note that the \$3 million held in central reserves in FY2007 was previously shown under III. Building and other expenditures.

Box 4. The Computation of Standard Costs for Staff Resources

- Until FY2002, the costs of staff in open-ended and limited-term positions were budgeted for in terms of staff years per department—not dollars. All personnel costs were paid out of centrally-held accounts.
- In FY2003, the concept of a standard cost for personnel was introduced into the dollar budgets of departments. The aim was to provide departmental budget managers with an estimate of the staff costs—their main cost of operation—and to provide flexibility in allocating different resources (staff, experts, contractual employees, travel and other costs) in the delivery of outputs.
- The use of a standard (rather than actual) cost ensures that departments have no financial incentive to differentiate between staff on the basis of salary level, gender, nationality, or benefit entitlement.
- The calculation of standard costs involves two steps: (i) the projection of the average salary for three groups of open-ended and limited-term staff (grades A1-A8, A9-A15, and B1-B5); and (ii) determination of average benefits relative to salaries in each group. Within the B1-B5 category, a separate calculation is made for Fund Executive Director employees, who have a lower and more variable (given the smaller number of staff) unit-cost than equivalently-graded staff.
- The average salary is calculated by taking the estimated total salary paid to each group for the present budget year, and dividing it by the assessed full-time equivalent in each group. This figure is then escalated by an assumed increase in salaries for the coming year.
- The average benefit is calculated by estimating the cost of the main benefits and allowances in the current budget year (including Medical Benefit Plan contributions, Staff Retirement Plan contributions, Group Life Insurance, home leave, education allowance, tax allowance, spouse and child allowance, and settlement allowances) and dividing it by the assessed FTEs in each group. The average estimated benefit is then escalated by the projected increase in the cost of such benefits in the coming year.

III. GROSS AND NET ADMINISTRATIVE EXPENDITURES

27. **The FY2008 central estimate of Fund receipts is \$71.4 million—a 4.5 percent increase over last year’s budget central estimate (Table 6).**⁴ This increase is mainly driven by a higher expected availability and drawdown of external financing, relative to FY2007. The main factors are as follows:

⁴ The central estimate of Fund receipts is the difference between the net administrative budget (financed from the Fund’s net income) and the Fund’s gross administrative expenditures (the budgetary aggregate relevant for the delivery of the Fund’s outputs).

- The third AFRITAC will come fully into operation next year: the associated administrative expenditures will be some \$5 million in FY2008, of which \$4.5 million will be externally financed by donors and the host country, accounting for most of the increase in receipts projected for FY2008. A further addition to external receipts will come with the new India Training Program.
- Other receipts items, however, including revenues generated from travel commissions and the Concordia apartments, are projected to be less buoyant in FY2008.
- Specifically, the projected travel commissions and rebates assume the continuation of the current budget figure (despite higher than expected receipts in FY2007). Given the uncertainty on future ticket purchasing arrangements, it seems prudent to assume a lower figure than the unexpectedly higher amounts collected in FY2007.
- The lower figure for receipts from the Concordia apartments reflects the need for a refit of certain apartments and thus reduced availability for rental.
- Over the remainder of the MTB period, the receipts from all sources are projected to remain broadly flat in nominal terms.
- The figures for external finance (predominantly for capacity building work) in FY2009 and FY2010 have been estimated following detailed consultations with OTM and each of the TA functional departments. All emphasize the considerable uncertainty on the projections. As noted above, a figure for external finance nearer the upper limit could raise the volume of capacity building work and its share of total Fund outputs.

IV. THE MEDIUM-TERM CAPITAL BUDGET

28. **Each year the Executive Board is asked to approve a capital appropriation for new building facilities and IT projects starting in the forthcoming budget year.** The appropriations have a three year lifetime: if a project is not completed, renewed Executive Board authority must be sought for any further expenditures. The capital budget is set within a three-year capital plan, that includes the start date and full cost of all capital projects envisaged over that period. Box 5 summarizes the main components of the capital budget.

29. **Executive Board approval is sought for an appropriation of \$46.6 million for capital projects beginning in FY2008 (Table 7).** The proposed appropriation would continue the downward trend in capital budget appropriations that began in FY2007 (Figure 2). The FY2008 capital budget appropriation is lower than the FY2007 appropriation; and the three-year capital plan for FY2008–FY2010 reflects a nominal reduction of 2.1 percent, or \$3.0 million, relative to the medium-term capital plan for FY2007–FY2009. To provide perspective, Table 8 and Figure 3 provide information on capital expenditures over the last ten years.

Table 6. Receipts, FY2007—FY2010
(In millions of U.S. dollars)

	FY2007 Central Estimate	FY2008		FY2009 Central Estimate	FY2010 Central Estimate
		Central Estimate	Upper Limit		
Externally Financed Technical Assistance	40.1	44.5	48.9	44.6	44.8
Direct Costs	35.6	39.4	43.4	39.6	39.6
Support Costs 1/	4.5	5.0	5.5	5.1	5.1
Scholarships (including administrative fees)	5.1	5.1	5.1	5.1	5.2
Fund-sponsored sharing agreements 2/	6.6	6.3	6.3	6.0	5.9
Publications income	4.0	4.0	4.0	4.1	4.1
Concordia apartment	2.7	2.1	2.1	2.4	2.6
Travel commissions	5.0	5.0	5.0	5.0	5.0
Other miscellaneous reimbursements 3/	2.6	2.4	2.4	2.4	2.2
Parking	2.1	2.0	2.0	2.0	2.0
Total	68.3	71.4	75.9	71.7	71.7

Source: Office of Budget and Planning.

Note: Figures may not add due to rounding.

1/ Includes the payments the Fund receives from donors towards administrative costs of providing externally financed technical assistance.

2/ Includes reimbursements principally from the World Bank for administrative services provided under sharing agreements, including the Joint Bank/Fund Library and the Bank/Fund Conference Office.

3/ Includes reimbursement from overseas offices and revenue and funding from a number of agreements with donors, interest and rent from HQ2 commercial leases.

Box 5. The Fund's Capital Budget: An Overview

The capital budget comprises projects under three categories: building facilities, information technology, and major building works.

- Building facilities comprise regulatory, replacement, and new facility projects. *Regulatory projects* are mandated by changes to building codes or industry regulations (e.g., changes in the fire code for office buildings), or are considered to be essential for the protection of Fund staff and property. *Replacement projects* provide for the replacement of building structures or equipment that is at the end of its useful life. *New facility projects* providing new functions or capacity within the existing headquarters building (such as the FY2002 reconfiguration of office and cafeteria space to accommodate the child care center) also fall under this category, but are less frequent.
- The purchase of information technology microcomputers, servers and other infrastructure equipment, and similar IT projects have been a part of the capital budget since FY1988. Since FY2000, the Executive Board approved the inclusion of major software development projects in the capital budget, in line with standard public and private sector practices.
- The construction of HQ2 was the only major building works project in recent years; none is planned looking forward.

The IT capital program in the Fund is overseen by the Chief Information Officer (CIO). He is supported directly in this capacity by the Committee on Business and Information Technology, a group of senior staff from various departments that is chaired by management, which assists in the review and prioritization of projects. The IT capital budget comprises four categories of project.

- Projects in the *Enterprise Information Program* are dedicated to the core work of the Fund, such as economic data management, document management and production, publications and information services (including communications), and economic and other data transfer with member countries.
- The *Administrative and Financial Information Program* comprises projects that enhance the Fund's administrative, financial and human resource application systems.
- Underpinning both of the above programs is the *Infrastructure and Connectivity Program*. Projects in this category are designed to sustain and improve the Fund's network, remote access capabilities, and overseas IT connectivity. This program also covers the purchase of new and replacement desktop and network computing equipment and communications links.
- *Strategic projects* are included in the IT Planning and Management Program. These are projects that affect the entire IT function, or that fundamentally shift the way in which IT is delivered.

The capital budget procedures in place have remained unchanged since the major reforms in FY2003. Project duration and funds are limited to three years, and funds lapse that are not spent within this time frame. For projects that extend longer than three years, it is necessary to make separate appropriations.

Cost benefit analysis (CBA) and other related requirements are applied to both major building works and major IT system development projects (with a value in excess of \$500,000). Even if projects qualify as eligible capital expenditures and have been satisfactorily appraised under a CBA and other tests, they are only included in the capital plan to the extent that the resource envelope allows.

Table 7. Medium-Term Capital Plans, FY2007–FY2008
(In millions of U.S. dollars)

	FY2007	FY2008	FY2009	FY2010	Total
	<u>FY2007 Current Plan</u>				
Building Facilities	19.8	20.6	14.3		54.7
Information Technology	28.3	26.0	32.0		86.3
Total	48.1	46.6	46.3		141.0
	<u>FY2008 Proposed Plan</u>				
Building Facilities		20.6	15.2	19.0	54.8
Information Technology		26.0	31.5	25.7	83.2
Total Requested		46.6	46.7	44.7	138.0

Source: Office of Budget and Planning.

Figure 2. Capital Budgets, FY2006-FY2010

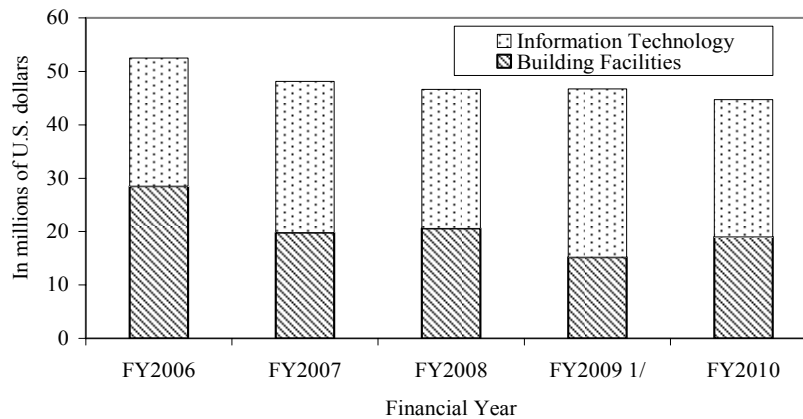


Table 8. Outturn and Projected Capital Expenditures, FY2000–FY2010 1/
(In millions of U.S. dollars)

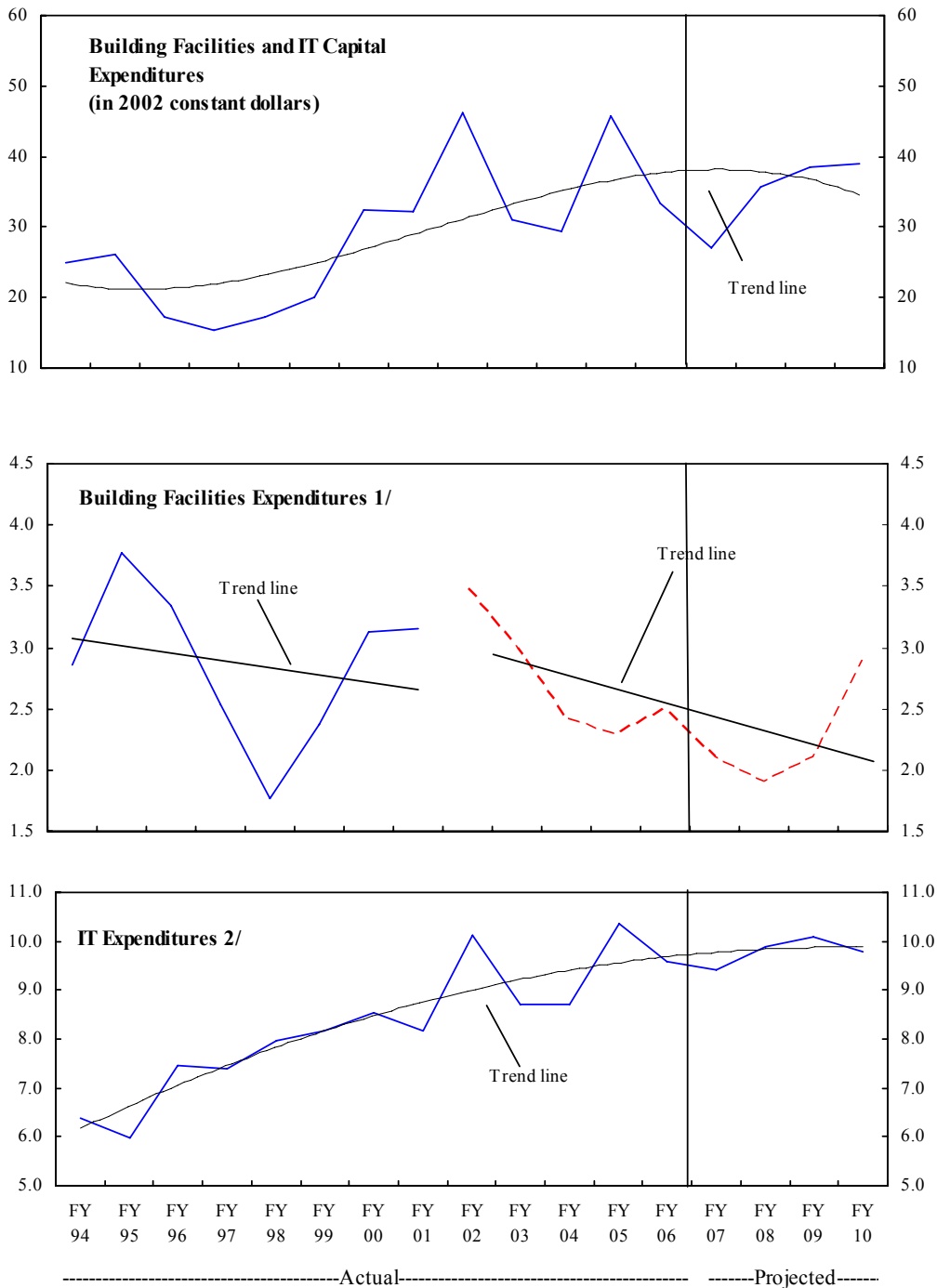
Major Program Area	Outturn						Estimated		Projected		
	FY2000	FY2001	FY2002	FY2003	FY2004	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010
Building Facilities	12.4	15.9	22.9	14.0	14.3	30.6	21.0	18.8	26.4	22.4	21.7
Budgets approved prior to FY2008	12.4	15.9	22.9	14.0	14.3	30.6	21.0	18.8	20.1	5.3	
FY2008 Budget									6.3	10.7	3.2
Medium-term FY2009-FY2010 Plan										6.4	18.5
Information Technology (IT)	18.6	15.8	30.7	24.8	21.5	34.2	26.9	25.4	29.4	31.7	30.0
Budgets approved prior to FY2008	18.6	15.8	30.7	24.8	21.5	34.2	26.9	25.4	16.6	4.7	
FY2008 Budget									12.8	11.6	1.5
Medium-term FY2009-FY2010 Plan										15.4	28.5
Total Building Facilities and IT	31.0	31.7	53.6	38.8	35.8	64.8	47.9	44.2	55.8	54.1	51.7
Major Building 2/	8.5	3.0	7.9	13.5	52.4	61.2	7.0	4.9	0.1	0.0	0.0
Budgets approved prior to FY2008	8.5	3.0	7.9	13.5	52.4	61.2	7.0	4.9	0.1	...	...
Total Capital Expenditures	39.5	34.7	61.5	52.3	88.2	126.0	54.9	49.1	55.9	54.1	51.7

Source: Office of Budget and Planning.

1/ Expenditures reflect disbursements against budget approvals, which for capital items have a life of three years.

2/ Includes HQ1 Phase III and HQ2.

Figure 3. Building Facilities and IT Expenditures, FY1994-FY2010



Source: Office of Budget and Planning.

1/ Three-year moving average as a percent of physical assets. Starting in FY2001 asset base included Phase III.

2/ As a percent of total IT administrative and capital expenditures to net administrative and capital budgets.

30. **The lower planned level of capital expenditures over the medium term, in part, reflects the near completion of security-related capital projects authorized by the Executive Board after the September 11 2001 attacks.** Investments to secure the Fund's overall business continuity plan were made in: (i) physical building security; and (ii) the IT High Availability program. These initiatives are in the final stages of completion; no further budget appropriation will be sought, beyond that already included in the FY2007–FY2009 medium-term capital plan.

31. **However, the appropriation proposed for FY2008 also reflects an intention to hold the capital budget broadly constant in nominal terms, while the two key benchmarks that have constrained the overall size of capital expenditures in recent years are reviewed.** Since FY2003, the overall size of the capital budget has effectively been capped relative to certain benchmarks. For building facility capital projects (very largely capital maintenance), the annual appropriations have been capped at 3 percent (on a moving average basis) of the asset value for the main headquarters building (HQ1)—an industry-wide norm for buildings of the age and type of HQ1. For total IT expenditures, a cap was set at 11 percent of the Fund's aggregate net administrative and capital budgets—a benchmark based on the practices of other major financial institutions. These benchmarks will continue to cap total capital appropriations for FY2008.

32. **Both benchmarks are now under review.** The 3 percent benchmark used to guide capital facilities spending on HQ1 needs to be reexamined in light of the addition of the HQ2 building to the Fund's physical asset base (although no significant capital maintenance spending is anticipated for some time). The benchmark presently used to guide total IT spending also needs to be reviewed given changes in the industry, such as increasing offshoring of the support for certain IT functions. Both benchmarks will be revised in FY2008 and a new approach will be used to guide the development of the FY2009–FY2011 medium-term capital plan. Thus, the proposals in Table 7 for new capital projects in FY2009 and FY2010 should be considered as provisional, subject to the completion of this review.

33. **In addition to assessing the overall size of the capital budget against external benchmarks, the FY2008—FY2010 capital budget and medium-term plan also reflect the continuing careful scrutiny of individual capital projects.** Building facility capital projects are evaluated based on need, urgency, and contribution to the life of the building. IT projects are evaluated on the strength of their cost-benefit analysis, and the return on investment, that they are expected to generate (Box 6 explains the considerations taken into account).

Box 6. The Assessment of Individual Capital Budget Projects

Determination of the Capital Budget Limits

The resource envelopes for the two ongoing components of the Fund's capital budget—IT and building facilities—have been derived with reference to benchmarks, as described in the text. However, these benchmarks establish upper limits and not the precise size of the budget needed. A valid business case has to be established for each and every project included in the capital plan.

Vetting Projects for Inclusion in the Capital Plan

All proposed IT projects are reviewed by the relevant IT committee in terms of their costs and benefits prior to being considered for inclusion in the IT medium-term capital plan. Of the \$102.6 million in IT capital projects submitted for FY2008—FY2010, this review reduced the request to \$84.0 million.

All IT projects (excluding equipment replacement) are subject to cost benefit analysis as follows:

- (i) an estimate of all costs by financial year over the useful life of the investment (including administrative, staffing, and capital costs) less the estimated terminal value of the investment at the end of its useful life;
- (ii) an estimate of all quantifiable benefits;
- (iii) a statement of all nonquantifiable or non-financial benefits;
- (iv) a statement of key assumptions, including calculations and price increase assumptions;
- (v) a discounting (net present value) of the costs and benefits for projects of \$1 million and greater, and a payback analysis for projects under \$1 million; and
- (vi) a sensitivity analysis by varying key assumptions and applying different discount rates.

For building facilities capital projects, a similar review mechanism to evaluate individual projects is not appropriate. Rather, TGS, as the Fund's facilities manager, identifies the scale and nature of the proposed project—whether driven by regulatory, security, capital maintenance or equipment redundancy considerations. Priorities are established in consultation with OBP.

Vetting Projects at the Time of Releasing Funds

Approved projects receive financing in tranches designed to match the needs of the project on the one hand, and the overall efficient use of budgetary resources on the other. Financing releases do not occur automatically, but instead require up-to-date information to be provided to OBP on the status of the particular project, including, where necessary, a revised cost-benefit analysis.

V. FINANCING ADMINISTRATIVE EXPENSES

34. **Table 9 brings together the proposals on the medium-term administrative and capital budgets described above, and translates them into the concept of administrative expenses as used in the Fund's financial statements.** The difference between the administrative and capital budgets, and the administrative expenses as in the Fund's financial statements, are described in Box 7. Table 9 also shows the impact of projected recorded administrative expenses on the Fund's net income in FY2007. The data in the Fund's financial statements are expressed in SDRs: to facilitate comparison, these data are converted to U.S. dollars in the table.

Table 9. Projected Net Income and Administrative Expenses, FY2007–FY2010
(In millions of U.S. dollars, unless otherwise indicated)

	Est. Outturn FY2007	Projected		
		FY2008	FY2009	FY2010
Net administrative budget	908	922	938	959
Add: Capital budget items not capitalized	26	29	27	35
Depreciation expense	33	34	35	36
A. Administrative expenses after capital-related adjustments	967	986	1,000	1,030
Percent change over previous year	3.5	2.0	1.4	3.0
B. Income sources	806	767	735	632
Income from lending operations 1/	358	231	200	111
Investment and other income	448	536	536	521
C. Income surplus/shortfall (B-A)	-161	-219	-265	-398
<i>Memorandum items:</i>				
Capital expenditures (budget definition)	49	56	55	52
Capital-related expenses (accounting definition)	59	63	62	70
Assumed U.S. dollar/SDR exchange rate	1.49	1.50	1.50	1.50

Sources: Office of Budget and Planning; and Finance Department.

Note: Figures may not add to totals due to rounding.

1/ Includes the margin for the rate of charge (108 basis points), surcharge income, and services charges.

Box 7. Administrative/Capital Budgets and Administrative Expenses

The Fund's administrative budget (used for budgeting purposes) differs from the concept of the Fund's administrative expenses (used for financial reporting purposes). Many institutions do not use the same concepts for budgeting and financial data, reflecting their different respective purposes. In line with established best practice, however, this box provides a reconciliation between the two concepts.

The definition of administrative expenses used by the Fund in its financial statements accords with International Financial Reporting Standards (IFRS). Two types of adjustment are required to translate from the administrative budget figures into administrative expenses: first to reflect an appropriate treatment of capital items; and second to capture certain accounting differences.

As regards capital expenditure, the administrative expenses reported under IFRS must include:

- depreciation expenses for capitalized assets; capital assets are depreciated over periods reflecting their useful lives: major buildings, such as HQ2, are depreciated over 30 years; IT equipment is depreciated over 3-5 years; and
- certain "capital" budget items, which are not capitalized under the Fund's accounting treatment, are expensed directly in administrative expenses in the year that the disbursements are made.⁵

35. The key points on administrative expenses are as follows:

- The FY2007 estimated outturn for capital budget expenditures is \$49 million. Of this, \$23 million will be capitalized on the Fund's balance sheet. The remaining \$26 million, which includes expenditures on renovations and repairs, security enhancements, and some IT development work, will be expensed directly.
- In addition, a depreciation charge of \$33 million related to assets capitalized in previous years will also be expensed.
- Thus, the capital element to be included in overall administrative expenses in FY2007 is \$59 million compared with the capital budget expenditure figure of \$49 million.
- With the projected outturn for the net administrative budget in FY2007 of \$908 million, administrative expenses, including capital-related adjustments, are thus estimated to be \$967 million.

⁵ Examples of such items include some repair work and those below a threshold of \$100,000.

36. **Thus, under the proposed administrative and capital budget, the Fund's administrative expenses are projected to increase at an average annual rate of 2.1 percent.**

37. **In the budget paper, staff are also required to provide estimates of the expenses associated with the administration of the Multilateral Debt Relief Initiative (No.1 Trust), Poverty Reduction and Growth Facility-Exogenous Shocks Facility Trust (PRGF-ESF) and the SDR Department.⁶**

- The estimated cost of administering the MDRI-I in FY2007 is SDR 2.3 million, compared to a budget estimate of SDR 1.7 million. For FY2008, the projected cost is SDR 1.6 million.
- The estimated cost of administering the PRGF-ESF Trust account in FY2007 is SDR 48.4 million, compared with a budget estimate of SDR 58.0 million. The projected cost for FY2008 is SDR 50.2 million.
- The estimated costs of administering the SDR Department in FY2007 is SDR 1.0 million, compared to a budget estimate of SDR 1.3 million. For FY2008, the projected cost is SDR 1.3 million.

⁶ Under Article V, Section 2(b). In recent years, the Board has decided not to seek reimbursement for the costs of administering the PRGF-ESF Trust.

VI. PROPOSED BOARD DECISIONS

1. **The following draft decisions, which may be adopted by a majority of the votes cast, are proposed for Executive Board approval.** Decision No. 1 sets out both a net budget and a ceiling on gross administrative expenditures that cannot be exceeded without Executive Board approval. Expenditures by the Executive Board and the Independent Evaluation Office, for which estimates are included in the budget, will be monitored and reported by OBP.

Decision No. 1

Administrative Budget for Financial Year 2008

1. Appropriations for net administrative expenditures for FY2008 are approved in the total amount of \$922,300,000.
2. A limit on gross administrative expenditures is approved in the total amount of \$998,200,000.
3. Any commitment going beyond the above amounts will be submitted to the Executive Board for approval.

Decision No. 2

Capital Budget for Projects Beginning in Financial Year 2008

1. Appropriations for capital projects beginning in FY2008 are approved in the total amount of \$46,600,000 and are applied to the following project categories.

I. Building facilities	\$20,600,000
II. Information technology	\$26,000,000