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United Nations

United Nations Relief and Works Agency for Palestine Refugees in the Near East

Financial report and audited financial statements

for the year ended 31 December 2012

and

Report of the United Nations Board of Auditors

General Assembly

Official Records
Sixty-eighth Session
Supplement No. 5C

A/68/5/Add.3

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Note

Symbols of United Nations documents are composed of letters combined with figures. Mention of such a symbol indicates a reference to a United Nations document.

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Letter of transmittal

30 June 2013

I have the honour to transmit to you the report of the Board of Auditors on the financial statements of the United Nations Relief and Works Agency for Palestine Refugees in the Near East for the year ended 31 December 2012.

(*Signed*) Amyas **Morse**
Comptroller and Auditor-General of the United Kingdom of
Great Britain and Northern Ireland
Chair of the Board of Auditors

The President of the General Assembly
of the United Nations
New York

Chapter I

Report of the Board of Auditors on the financial statements: audit opinion

Report on the financial statements

We have audited the accompanying financial statements of the United Nations Relief and Works Agency for Palestine Refugees in the Near East for the year ended 31 December 2012, which comprise the statement of financial position, the statement of financial performance, the statement of changes in net assets/equity, the statement of cash flow, the statement of comparison of budget and actual amounts, and the explanatory notes.

Responsibility of management for the financial statements

The Commissioner-General is responsible for the preparation and fair presentation of these financial statements, in accordance with the International Public Sector Accounting Standards. This responsibility includes: designing, implementing and maintaining internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Responsibility of the auditors

Our responsibility is to express an opinion on these financial statements on the basis of our audit. We conducted our audit in accordance with the International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

An audit includes the performance of procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor’s judgement and include an assessment of the risk of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the entity’s preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity’s internal controls. An audit also includes an evaluation of the appropriateness of the accounting policies used and the reasonableness of the accounting estimates made by management, as well as an evaluation of the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the United Nations Relief and Works Agency for Palestine Refugees in the Near East as at 31 December 2012 and the financial performance and cash flows for the year then ended, in accordance with the International Public Sector Accounting Standards.

Report on other legal and regulatory requirements

In our opinion, the transactions of the United Nations Relief and Works Agency for Palestine Refugees in the Near East that have come to our notice or that we have tested as part of our audit have, in all significant respects, been in accordance with the Financial Regulations of the United Nations Relief and Works Agency for Palestine Refugees in the Near East and legislative authority.

In accordance with regulation 12.2 of the Financial Regulations of the United Nations Relief and Works Agency for Palestine Refugees in the Near East and the related annex, we have also issued a long-form report on our audit of the Agency.

(*Signed*) Amyas **Morse**
Comptroller and Auditor-General of the United Kingdom of
Great Britain and Northern Ireland
Chair of the Board of Auditors

(*Signed*) Ludovick S. L. **Utouh**
Controller and Auditor-General of the United Republic of Tanzania
(Lead Auditor)

(*Signed*) **Liu** Jiayi
Auditor-General of China

30 June 2013

Chapter II
Long-form report of the Board of Auditors

Summary

The Board of Auditors has audited the financial statements and reviewed the operations of the United Nations Relief and Works Agency for Palestine Refugees in the Near East (UNRWA) for the year ended 31 December 2012. The audit was carried out at the UNRWA headquarters in Amman and through visits to the field offices in the West Bank and the Gaza Strip.

Audit opinion

The Board issued an unqualified audit opinion on the financial statements of UNRWA for the year ended 31 December 2012. The Board's opinion is set out in chapter I of the present report.

Overall conclusion

The Board identified weaknesses in financial management and non-compliance with financial regulations in the conduct of business both at headquarters and at field offices.

The Board has made a number of recommendations aimed at improving controls over procurement and contract management, asset management, cash and treasury management, and information technology.

The Board found that UNRWA has not yet implemented 10 (28 per cent) of its previous recommendations and identifies similar weaknesses in the present report. UNRWA therefore needs to improve controls and compliance in order to ensure the efficient and effective delivery of its services.

The initial implementation of the International Public Sector Accounting Standards (IPSAS) accounting framework in 2012 was a major achievement of UNRWA. The Board noted, however, that UNRWA had experienced a number of difficulties with the implementation that required remedial action before the financial statements were finalized. UNRWA now faces the challenge of improving systems, decision-making processes and financial management to realize the wider benefits of the new financial information provided under IPSAS.

Key findings

The Board identified a number of issues that require the consideration of management, in particular those set out below.

Follow-up of previous recommendations

Of the 36 recommendations made for the biennium 2010-2011, 26 (72 per cent) had been fully implemented and 10 (28 per cent) were under implementation. The Board encourages UNRWA to expedite the implementation of the remaining recommendations.

Evaluation of going concern

UNRWA, like many other United Nations entities, depends heavily on voluntary contributions from Member States and other donors to support the delivery of its mandate. In its previous report (A/67/5/Add.3), the Board reported on the going-concern risks that the Agency was facing owing to the depletion of its reserves. The Board notes that while over the past two reporting periods there has been a gradual increase in the level of contributions, expenses have also increased. In 2012, UNRWA reported a deficit of $47.45 million. The Board also notes that current assets exceeded current liabilities by $203.72 million, enabling the Agency to meet its current obligations as they fall due. The Board further notes that UNRWA has developed a resource mobilization strategy and foresees a modest increase in funding from traditional donors, while also seeking to expand its donor base to include the emerging donor countries and the private sector. In the light of the foregoing, the Board is of the view that UNRWA is a going-concern entity for the foreseeable 12 months from the reporting date.

Review of financial statements

The Board's review of the first approved financial statements submitted for audit purposes noted that a number of account adjustments were required in order to ensure that the financial statements were fairly stated. The deficiencies included, for example, improper reclassification of some balances, improper classification of expenses and non-disclosures. These deficiencies were rectified, but the Board is of the view that UNRWA needs to improve the process of compiling IPSAS financial information.

End-of-service employee benefits

The Agency's statement of financial position discloses total liabilities of $599.86 million, of which $463.02 million (77 per cent) relates to area staff end-of-service benefits. "Area staff end-of-service benefits" refers to consideration given by the Agency at the end of service in exchange for service rendered by employees in accordance with the staff rules and regulations. The Agency's after-service health insurance liabilities for other international staff are borne by the United Nations. The Board's concern relates to the magnitude of the reported area staff end-of-service employee liability of $463.02 million, which is currently an unfunded obligation. In its previous report (A/67/5/Add.3, chap. II, paras. 52-54), the Board pointed out the need to establish a funding strategy. UNRWA discloses in note 15 to the financial statements that end-of-service liabilities are unfunded and will continue to be so in the future. The Board is of the view that UNRWA needs to reconsider its funding strategy.

Financial overview

For the period under review, total revenue was $944.14 million and total expenses amounted to $991.59 million, resulting in a deficit of $47.45 million. The deficit was attributed mainly to depreciation expenses of property, plant and equipment amounting to $22.93 million and interest and service costs of $67.58 million, which are non-cash expenses. As at 31 December 2012, UNRWA had total assets of $806.5 million and total liabilities of $599.86 million. Of its total assets, $232.43 million represented balances in cash and cash equivalents. The net current asset balance was $203.72 million, resulting from current assets of $358.82 million and current liabilities of $155.1 million.

The financial position of UNRWA as at 31 December 2012, which is determined using financial indicators such as ratios, shows that UNRWA has good short-term financial strength, with assets exceeding liabilities and sufficient cash to ensure a good liquidity position.

Management of assets

The Board noted that UNRWA had automated its assets register but that, owing to delays in reconciling the register to corresponding figures in the general ledger, some $5.44 million of assets had not been recorded in the fixed-assets register at year-end. The Board also found that UNRWA operates its field offices in 547 buildings and 693 plots leased from Governments and private owners but lacks legal occupancy documents for 41 buildings and 255 plots.

The Board also noted that of the $183.45 million in contingent liabilities disclosed in the financial statements, $0.04 million (0.02 per cent) comprised claims from landlords from whom the Agency rents buildings. Although the amount claimed against the Agency is insignificant, UNRWA risks eviction from the buildings subject to applicable laws relating to improper occupancy; at the same time, it does not have adequate alternative accommodation should this risk materialize.

Inventory management

The Agency classified some of its consumable stores, maintenance materials and spare parts for consumption as non-inventory items. The Board had raised concerns about the lack of clear definitions in the existing policy on inventory and recommended the need for a clearer policy on this matter. However, it found that inventory items with a total acquisition value of $0.542 million were incorrectly categorized as non-inventory owing to the lack of a clear policy for the definition of the two categories of inventory.

Microfinance Department

The Board's review of the Microfinance Department operations in the Syrian Arab Republic noted that as at 31 December 2012, UNRWA operations in the Syrian Arab Republic had a loss of $3.64 million, with operational self-sufficiency of only 29.5 per cent. The operational self-sufficiency percentage measures how well the Department covers its costs through its operating activities. It indicates that the current level of operational self-sufficiency is inadequate to cover the Agency's running costs in the Syrian Arab Republic.

Recommendations

The Board made several recommendations on the basis of its audit. The main recommendations are that UNRWA:

(a) Strengthen its controls to ensure that the system of processing, reviewing and summarizing financial information is more reliable and adequate for the preparation of its financial statements;

(b) Develop a budgeting strategy for enhancing the funding of employee end-of-service liabilities;

(c) Develop a clear monitoring mechanism for supplier performance during the contract period. This will ensure compliance with regulations and will give management assurance that poor supplier performance is being addressed;

(d) Improve the internal checking mechanisms with respect to the timely completion of the electronic asset register and perform regular reconciliations with the general ledger;

(e) Obtain relevant documents to substantiate the right of use of the buildings and plots occupied by UNRWA;

(f) Set timelines for the development of a clear inventory policy, which needs to conform with the requirements of International Public Sector Accounting Standards 12.12;

(g) Enhance the monitoring of the loan portfolio in the Syrian Arab Republic with a view to improving its operational self-sufficiency targets, in order to ensure that its operational costs are sustained in a reliable manner.

A. Background information

1. The United Nations Relief and Works Agency for Palestine Refugees in the Near East (UNRWA) was established by the General Assembly by its resolution 302 (IV) of 8 December 1949 and became operational on 1 May 1950. It is a subsidiary organ of the Assembly within the United Nations system.

2. The mission of UNRWA is to help Palestine refugees to achieve their full potential in terms of human development under difficult circumstances, consistent with internationally agreed goals and standards. The Agency is one of the largest United Nations programmes, serving a population of 4.8 million Palestine refugees in the Gaza Strip, the West Bank, Jordan, Lebanon and the Syrian Arab Republic.

3. UNRWA is also one of the largest employers in the Middle East, with some 30,225 staff, most of whom are Palestine refugees. UNRWA has schools accommodating approximately 480,000 children and 22,000 education staff, as well as 137 health centres across the region serving 10 million patients annually. The Agency also assists some 280,000 of the poorest and most vulnerable refugees with special needs, such as people with disabilities.

B. Mandate, scope and methodology

4. The Board of Auditors has audited the financial statements of UNRWA and has reviewed its operations for the year ended 31 December 2012 in accordance with General Assembly resolution 74 (I). The audit was conducted in conformity with regulation 12.2 of the Financial Regulations of UNRWA and the International Standards on Auditing. The latter standards require that the Board comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

5. The audit was conducted primarily to enable the Board to form an opinion as to whether the financial statements present fairly the financial position of UNRWA as at 31 December 2012 and its financial performance and cash flows for the year then ended, in accordance with the International Public Sector Accounting Standards (IPSAS). This included an assessment as to whether the expenses recorded in the financial statements had been incurred for the purposes approved by the governing body and whether revenue and expenses had been properly classified and recorded in accordance with the Financial Regulations of UNRWA. The audit included a general review of financial systems and internal controls and a test examination of the accounting records and other supporting evidence to the extent that the Board considered necessary to form an opinion on the financial statements.

6. The Board also issued a separate unmodified audit opinion on the financial statements of the UNRWA Area Staff Provident Fund for the year ended 31 December 2012, prepared in accordance with the International Financial Reporting Standards.

7. Furthermore, the Board performed an annual audit of the Microfinance Department and issued an unmodified opinion on its financial statements for the year ended 31 December 2012.

8. In addition to the audit of the financial statements, the Board carried out reviews of UNRWA operations in accordance with regulation 7.5 of the Financial

Regulations of the United Nations. This allows the Board to make observations with respect to the efficiency of the financial procedures, accounting system, internal controls and administration and management of UNRWA operations. The General Assembly had also requested the Board to follow up on previous recommendations and to report to it accordingly. Those matters are addressed in the relevant sections of the present report, and a summary of the results is included in annex I.

C. Findings and recommendations

1. Follow-up of previous recommendations

9. Of the 36 recommendations made for the biennium 2010-2011, 26 (72 per cent) had been fully implemented and 10 (28 per cent) were under implementation. The Board encourages UNRWA to improve the pace of implementation. Details of the status of implementation of these recommendations are shown in annex I.

10. The Board is concerned that one recommendation made in 2002-2003, relating to the testing, finalization and approval of the UNRWA disaster recovery plan, remains unimplemented.

2. Financial overview

11. Total revenue and income for the period under review amounted to $944.14 million, while total expenses amounted to $991.59 million, resulting in a deficit of $47.45 million. The Standards allow the entity adopting IPSAS in the first year to ignore comparative information for the prior period. Accordingly, the comparative figures have not been provided in the statement of financial performance. Details of financial performance by fund are summarized in table II.1.

Table II.1
Financial performance by fund
(Thousands of United States dollars)

	Unearmarked activities	*Earmarked activities*					
Item	*General Fund*	*Restricted funds*	*Microfinance Department*	*Emergency appeals*	*Projects*	*Inter-fund balances*	***Total***
Total revenue and income	586 976	32 768	7 761	164 498	174 101	(21 963)	**944 141**
Total expenses	664 039	46 155	10 226	166 721	125 993	(21 542)	**991 592**
Surplus/(deficit) for the year	**(77 063)**	**(13 387)**	**(2 465)**	**(2 223)**	**48 108**	**(421)**	**(47 451)**

Source: UNRWA financial statements for the year ended 31 December 2012.

12. All funds closed with deficits except the project fund, which closed with a surplus of $48.11 million. The reported deficit of $77.06 million in the General Fund, equivalent to 13 per cent of the funds received, was attributed mainly to non-cash expenses of $67.58 million and $22.93 million in respect of severance and depreciation expenses, respectively.

13. A deficit of $13.39 million (41 per cent) relating to restricted activities resulted from the matching of income received during the year against the related expenses.

The restricted fund expenses were based on the fund balance of $26.60 million as at 31 December 2011, with a closing balance of $16.06 million on 31 December 2012. On the other hand, the fund for emergency appeals closed with a deficit of $2.22 million. The closing fund balance for the emergency fund was $32.52 million, as reflected in note 32 to the financial statements (position by fund). In addition, cash held at the bank decreased to $232 million, compared with the $270 million reported for the previous biennium, reflecting a decrease of $38 million, or 14 per cent.

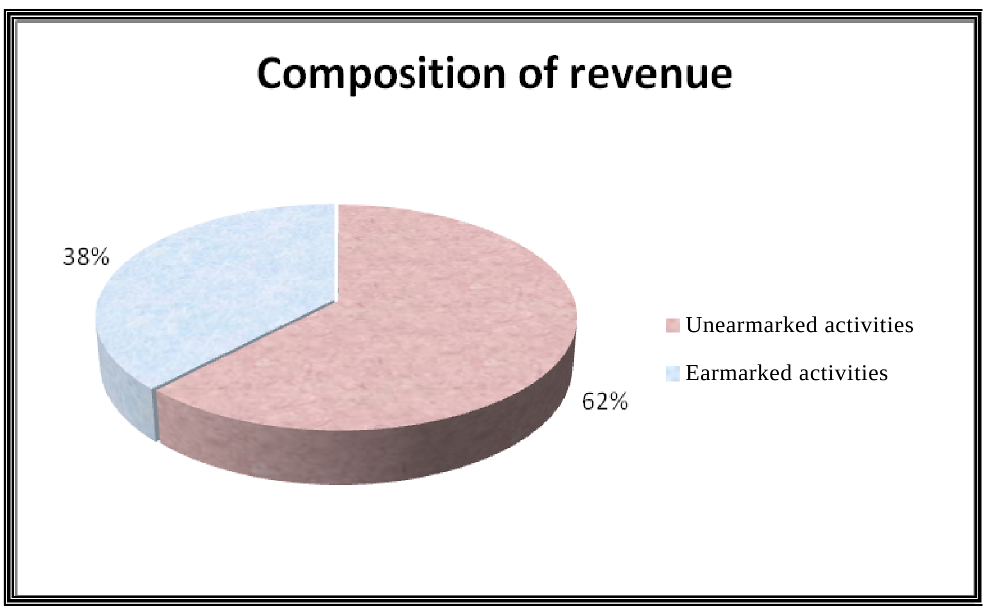
14. The property, plant and equipment balance increased by $22.94 million (equivalent to 6 per cent), from $414.83 million for 2011 to $437.77 million for 2012. The increase is explained by additions of $48.12 million and depreciation of $22.93 million.

15. Employee benefits increased by $54.49 million (equivalent to 12 per cent), from $442.72 million in 2011 to $497.22 million in 2012. The increase was attributed mainly to recognition of severance expenses of $67.56 million, an actuarial loss of $11.56 million and payment of $28.67 million made during the year.

Analysis of revenue

16. The Agency's activities comprise unearmarked activities financed through the General Fund and earmarked activities financed through the restricted funds, emergency appeals, the projects fund and the Microfinance Department fund. Total revenue received for unearmarked activities was $586.98 million, equivalent to 62 per cent of total contributions, while funds for earmarked activities amounted to $357.17 million, or 38 per cent of total funds received during the year.

Fund allocation by activities



Agency sources of revenue

17. With the exception of international staff posts, which are funded from the United Nations regular budget through assessed contributions and posts provided by other

United Nations agencies, the ongoing operations, projects and emergency appeals of UNRWA are funded through donors' voluntary contributions. During the year ended 31 December 2012, $882.76 million in voluntary contributions (96 per cent of total contributions of $919.57 million) was received. The remaining $36.81 million (4 per cent) was received from the United Nations regular budget for international staff, as reflected in notes 20 and 21 to the financial statements.

Expense analysis

18. A significant amount of the Agency's costs comprises wages, salaries and employee benefits, which amounted to $591.39 million, equivalent to 60 per cent of total expenses of $991.59 million, for 2012. Of the reported staff costs, $497.56 million, equivalent to 84 per cent, related to area staff basic salaries and allowances, while $38.24 million (6.5 per cent) related to international staff and $49.70 million (8.4 per cent) covered Agency contributions to the Area Staff Provident Fund. Health-related expenses constituted $5.90 million (1 per cent) of total staff costs.

3. Evaluation of going concern (financial health)

19. UNRWA depends heavily on voluntary contributions from Member States and other donors to support the delivery of its mandate. In its previous report (A/67/5/Add.3), the Board reported on the going-concern risks that UNRWA was facing owing to the depletion of reserves to a very low level. The Board notes that while there has been a gradual increase in contributions over the past two reporting periods, increased expenses still led to a deficit of $47.45 million in 2012.

20. The Board also notes that current assets exceed current liabilities by $203.72 million, with a current ratio[1] of 2.3:1, implying that UNRWA could meet its current obligations when they fall due. UNRWA has developed a resource mobilization strategy and foresees a modest increase in funding from traditional donors in 2013; it also aims to expand its donor base to include emerging donor countries and the private sector. In the light of the foregoing, the Board is of the view that UNRWA is a going concern for the foreseeable 12 months from the reporting date (31 December 2012).

4. Review of financial statements

21. In its previous report, the Board noted areas of improvement in the Agency's financial statement preparation process, but recommended that UNRWA strengthen its controls over the preparation and review of its financial statements.

22. The Board's review of the first approved financial statements submitted for audit purposes identified deficiencies in presentation, including the following:

(a) Reclassification of payable to receivable balances amounting to $2.06 million;

(b) Netting-off of payables against receivables amounting to $1.18 million and $2.93 million, respectively;

(c) Revenue amounting to $2.99 million was netted off against expenses of $3.4 million;

[1] "Current ratio" means the ratio of current liabilities to current assets and measures how reliably the maturing short-term obligations can be met from current assets.

(d) Inventory amounting to $0.542 million was treated as non-inventory and expensed on the date of purchase.

23. All deficiencies were rectified by UNRWA except expensed inventory amounting to $0.542 million, which did not materially affect the fair presentation of the financial statements. The Board considers that the deficiencies in the presentation of the financial statements were a result of inadequate preparation for the adoption of IPSAS.

24. **UNRWA agreed with the Board recommendation that it strengthen its controls to ensure that the system of processing, reviewing and summarizing financial information is more reliable and adequate for the preparation of its financial statements.**

25. UNRWA stated that the monthly/yearly instructions and timetable for the closure of accounts and the preparation of financial statements had been implemented. In addition, the Agency had made changes to its financial statement grouping schedule in accordance with IPSAS requirements, and was in the process of updating the financial statement coding in the current, RAMCO system so that the financial statements might be automatically generated from the system, thus eliminating the need for manual adjustments.

Ineffective generation of financial data through the RAMCO system

26. RAMCO is an enterprise resource planning system. It has a financial management system module that UNRWA uses to gather financial data from various departments and to generate financial reports such as the general ledger and trial balance (a list of all the general ledger accounts contained in the ledger of a business, with the name and the value of the nominal ledger account).

27. The Board noted that the process of producing financial statements involves the extraction of the trial balance from the financial management system, with the accounting staff correcting errors manually using Excel spreadsheets to align the financial statements with the IPSAS reporting framework. Therefore, the lack of a centrally controlled, automated application causes some difficulties in information-sharing and in maintaining consistency in the naming of accounts, as well as incorrect processing and treatment of some account balances.

28. UNRWA is in the process of replacing its RAMCO system with a new enterprise resource planning system, expected to be operational by December 2014. The Board considers this to be an important and critical move that involves learning from the past and improving for the future, a positive approach to solving the current problem.

29. **UNRWA agreed with the Board’s recommendation that it: (a) ensure that the implementation of the new enterprise resource planning system takes into consideration the full automation of all critical processes, including the generation of financial statements; and (b) enhance the process of managing versions of accounting information produced for end-users to avoid the confusion caused by differing naming conventions and inaccurate aggregation of data.**

30. UNRWA stated that it had included the financial processes in the enterprise resource planning project and that it would review the process of managing versions of accounting information in order to identify any enhancements that might be needed.

5. Accounts receivable

Lack of a follow-up strategy with respect to value-added tax receivable

31. The Board noted that UNRWA recognized in its statement of financial position a sum of $49.08 million in respect of accounts receivable net of provision. Of this amount, $41.73 million, equivalent to 84 per cent, comprised value-added tax receivable from the Palestine Authority and Israel. As at year-end, UNRWA had value-added tax provisions amounting to $34.91 million and $1.24 million in provisions for other receivables.

32. The Board noted that UNRWA, in line with its accounting policy, had made provision for the entire amount of value-added tax receivable outstanding ($11.87 million), which had accrued for periods ranging from 6 to 16 years ago (from 1996 to 2006). The Board, however, found no evidence of any strategy for collecting the outstanding value-added tax from the respective Governments. Given the financial constraints facing the Agency, a follow-up strategy is important to improve its financial position.

33. **UNRWA agreed with the Board's recommendation that it develop a strategy for the recovery of the long-outstanding value-added tax receivable.**

34. UNRWA informed the Board that it was strengthening its efforts to request such recovery from the Palestinian Authority and that it had planned to seek exemptions to avoid the accumulation of additional value-added tax in the future.

Lack of authorization limits for write-off of bad debts

35. The Board noted that current UNRWA policies and procedures authorize the Director of Finance to write off receivables that have remained uncollectible for a certain period. For example, the Director has unlimited authority to write off all value-added tax receivable that has remained uncollected after a period of six years, and all other receivables that have remained uncollected for three years. The Board noted that during the period under review, bad debts amounting to $1.04 million had been written off by the Director of Finance, whereas the highest individual amount written off during the year had been $0.54 million. While the Board welcomes the clarification by management of these policies and procedures, it is concerned that this unrestricted power might compromise the overall adequacy of internal control.

36. The Board is of the view that the power of the Director of Finance to write off amounts receivable should be capped at a certain level beyond which the sanction of a higher authority such as the Advisory Committee on Internal Oversight should be required.

37. **The Board recommends that UNRWA consider reviewing the existing policy and establish levels of write-off power, designating a different authority, preferably the Advisory Committee on Internal Oversight, to sanction write-offs whenever the amount involved is significant.**

38. UNRWA informed the Board that it considers the current levels of authority to be appropriate. However, the Board considers that the internal control is weak

owing to the inadequate segregation of duties, and therefore that the write-off power should be reviewed in order to involve a different authority in the approval process.

6. End-of-service employee benefits

39. The Agency's statement of financial position discloses total liabilities of $599.86 million, of which $463.02 million (equivalent to 77 per cent) relates to end-of-service benefits of local staff hired within the country of operation (area staff). "Area staff end-of-service benefits" refers to consideration given by the Agency at the end of service in exchange for service rendered by employees in accordance with the staff rules and regulations. UNRWA also disclosed an amount of $2.23 million for after-service health insurance, leave liability and repatriation grant for international staff, which are funded by the United Nations Secretariat.

40. The Board is concerned at the magnitude of the reported unfunded obligation of area staff end-of-service benefits of $463.02 million. In its previous report, the Board pointed out the need to establish a funding strategy. However, UNRWA states in note 15 to the financial statements that end-of-service liabilities will remain unfunded for the foreseeable future. The Board continues to note that that Agency's current financial position and the absence of a strategy for funding these liabilities are indications of the inability of UNRWA to settle the whole amount of staff liabilities in the event that it should cease to operate.

41. **The Board reiterates its previous recommendation that UNRWA develop a funding strategy to enable it to honour all of its end-of-service liabilities.**

7. Review of Finance Manual and Financial Regulations

42. If an organization is to be able to adopt IPSAS, continue its day-to-day operations and report its results efficiently, any existing instruments such as financial regulations, rules, guidance manuals and related policies and procedures must be revised and aligned with the new reporting framework in a timely manner.

43. Effective 1 January 2012, UNRWA migrated from the United Nations system accounting standards to IPSAS. However, the Board noted that in carrying out its business and, eventually, the preparation of its financial statements, the Agency had used draft financial regulations prior to consulting the Advisory Committee on Administrative and Budgetary Questions and the Secretary-General, in accordance with paragraph 9 (c) of resolution 302 (IV). The financial regulations were approved retrospectively in July 2013. While the new Financial Regulations did not conflict with IPSAS requirements, UNRWA has not clearly informed the Board as to why they were not submitted to the Advisory Committee and the Secretary-General in a timely manner. The Board considers that the process of approving the Regulations was an important activity that should have been completed within the time frame established for IPSAS preparations.

8. Procurement and contract management

Tender evaluation team was not properly appointed and failed to confirm the absence of conflicts of interest

44. The Board noted that the UNRWA Procurement Manual provides guidance on how tender evaluation teams can be appointed by empowering the Chief of the Procurement and Logistics Department, at headquarters, and field procurement and

logistics officers to appoint evaluation teams for operations falling under their authority. However, the Manual does not specify precisely which method and process are to be followed by the appointing authority. For example, at the Jordan field office, the members of the evaluation team were not given formal appointment letters to confirm their qualifications to carry out tender evaluations. In addition, the Board noted that the team members had not declared whether they had any conflicts of interest, contrary to the requirements set out in chapter 8.4.1, paragraph 5, of the Procurement Manual, but compliance had not been enforced.

45. The Board is of the view that, to ensure transparency, fairness and the integrity of tender evaluation team appointments, a method of appointment should be properly defined in the manual. In addition, to strengthen the accountability of evaluation team members for their actions and decisions, it is important that they be appointed through formal appointment letters and that they declare and document whether they have identified any conflicts of interest that might preclude their taking part in the evaluation exercise.

Lack of specified contract start and completion dates

46. Chapter 10.2 (1) of the UNRWA Procurement Manual requires that every contract between UNRWA and a supplier include, in the main body of the contract, a proviso indicating the type of contract, period of performance, points of contacts, specific dates and notice addresses. In addition, according to paragraph 10.2.1 (6) of the Manual, all contracts should precisely define start and completion dates, as well as milestones for successful performance.

47. From our review of contract management at the Jordan field office, we noted that most contracts fully complied with the Procurement Manual; however, two of the seven contracts selected for testing (one for refuse removal and another for Internet service) did not indicate clearly their start and completion dates.

48. Management stated that the duration of each contract was indicated in the standard clause “shall end upon completion of the last obligation arising hereunder”, whose meaning was clear, even if the specific completion date was not indicated. However, the Board is of the view that using “completion of the last obligation” to mean the end of a contract is likely to lead to disputes if contractual obligations are finalized beyond the expected time frame, and does not provide management with a good basis for enforcing the contractor’s compliance in the event of time and cost overruns.

49. **UNRWA agreed with the Board’s recommendation that it consider the revision of all service contracts to clearly specify their start and completion dates in order to ensure compliance and enforceability.**

50. UNRWA stated that it did not consider the problem to be system-wide and that to review all contracts would be onerous. The Board reiterates the need for the specification of start and completion dates in the service contracts to avoid legal risks.

Lack of pre-bid conferences or site visits for interested bidders

51. According to chapter 7.5.1, paragraphs 3, 4 and 4 (a), of the UNRWA Procurement Manual, “For technically complex acquisitions, a pre-bid conference between UNRWA and the suppliers could be held in addition to, or instead of,

issuance of written clarifications. Such a conference may be in the form of a meeting or a pre-bid site inspection."

52. From our review of 10 construction contracts, amounting to a total of $2.3 million, at the Jordan field office, we noted that neither joint pre-bid conferences nor site inspections had been conducted and that no justification for waiving the conferences/inspections had been documented in respect of the construction projects awarded to suppliers, contrary to chapter 7.5.1, paragraphs 3, 4 and 4 (a), of the UNRWA Procurement Manual.

53. A pre-bid conference or site inspection enables bidders to receive clarifications regarding solicitation documents and scopes of work and to gain an understanding of the complexities of the work involved. In addition, pre-bid conferences and site inspections enhance competition and give bidders equal opportunity by providing them with relevant information at the site. The lack of a pre-bid conference or site inspection could limit bidders' equal understanding of the work involved, as some suppliers might have an information advantage over others and therefore the contract award might not achieve best value for money.

54. UNRWA stated that it would conduct pre-bid site inspections/pre-bid meetings for large projects that were complex in terms of design or site.

55. **UNRWA agreed with the Board's recommendation that it: (a) ensure that pre-bid site visits and the subsequent pre-bid meetings are conducted with a view to the transparent, fair and competitive tendering of all major/complex contracts; and (b) ensure that whenever a pre-bid site inspection/pre-bid meeting is not practicable, the rationale is properly documented.**

56. While agreeing with the Board's recommendation, UNRWA does not consider this problem to be systematic or Agency-wide. The Board will continue to review the bidding process across the mission's field offices.

Monitoring of service and construction contracts

57. Chapter 4.4, paragraph 3, of the UNRWA Procurement Manual states, "To promote economical and efficient procurement, the performance of existing suppliers should be evaluated on an ongoing basis."

58. The Manual also requires that proper records be maintained by procurement staff at headquarters and field offices regarding the performance of each supplier in order to identify underperformers. Underperformers are to be flagged, and information regarding the nature of the underperformance is to be discussed with the Chief of the Procurement and Logistics Department.

59. UNRWA has established a procurement and inventory management system module that is integrated with the RAMCO financial management system for recording and monitoring procurement activities. UNRWA uses the system to facilitate the evaluation of vendor performance in terms of the quality of the service delivered during and after the contract period. However, the monitoring of service and construction contracts is conducted manually, and the system does not therefore capture procurement information for service and construction contracts, nor is the evaluation of the performance of suppliers recorded in the system.

60. The monitoring and evaluation of construction contracts outside the system are based on construction phases or milestones as defined in the contract agreement.

However, the Board noted that in the case of service contracts, it had been difficult to ascertain the performance of vendors, owing to the absence of a clear tracking system during the contract period.

61. Management stated that as the current information technology application did not have sufficient provision to ensure the proper supervision of service delivery, a decision had been taken to include and implement the requirement through the new enterprise resource planning solution, which would be implemented in 2013.

62. **The Board recommends that UNRWA develop a clear mechanism for monitoring supplier performance during the contract period. This will ensure compliance with regulations and will give management assurance that poor supplier performance is being addressed.**

63. UNRWA stated that it agreed in part with the Board's recommendation, explaining that it had established a data-gathering tool that facilitates the use of key performance indicators for suppliers of goods on the basis of which performance can be measured and corrective action taken. With respect to services and construction, UNRWA stated that it would be costly to introduce such a system, and that in 2014 it planned to introduce a new tool that would cover both goods and services. For the time being, the Agency is planning to extend the tool used for goods to cover services and construction. The Board will verify the measures being taken, but it reiterates the need for a clear and efficient monitoring mechanism.

The use of inappropriate waivers of the procurement process in awarding contracts

64. Chapter 5.4.1 of the UNRWA Procurement Manual stipulates the circumstances in which waivers of the competitive procurement process are acceptable and that the reasons for such waivers must be recorded in writing.

65. In its previous report, the Board reviewed the process of granting waivers of competitive procurement and noted a number of instances in which it had not been in accordance with the Agency's policies and procedures. It recommended to UNRWA that it: (a) conduct a review to establish the reasons for the high number of waivers; (b) implement processes to monitor the use of waivers; and (c) adequately document and justify the use of waivers.

66. During our visit to the Jordan field office, we noted a number of improvements. Currently, UNRWA documents reasons for waivers for each contract. However, from a review of seven contracts, we noted that three were supported by reasons that were not consistent with the requirements set out in the Procurement Manual. For example, a $33,900 cleaning contract had been renewed on the grounds of satisfactory performance on the part of the service provider, without any evidence that a performance evaluation had been undertaken.

67. **The Board recommends that UNRWA continue to review the process of granting waivers and that it remind staff of the need to ensure that they are in line with the requirements set out in the Procurement Manual.**

68. UNRWA stated that it agreed in part with the observation made, and informed the Board that it had rewritten and reissued the provisions regarding waiver documents in version 2 of the Procurement Manual. It had also introduced a revised waiver form and included a functionality in the vendor and logistics system that allowed the reasons for waivers to be systematically recorded and analysed. The

Board acknowledges the improvement made, but it considers that there is a need for UNRWA to monitor compliance across the Agency.

9. Management of assets

High number of buildings in bad condition

69. Our review of property, plant and equipment records confirmed that UNRWA had obtained valuations of its land and buildings through the use of consultants and its own building experts and surveyors from 2008 to 2011. At 31 December 2012, UNRWA held property assets with a total net book value of $366.8 million.

70. Valuation reports showed that UNRWA had 59 buildings classified as dilapidated and beyond repair and 434 buildings classified as in need of repair. This abnormally high number of assets in bad condition requires the allocation of sufficient resources to avoid further deterioration and loss. On average, the amount of resources allocated to repair one building is $2,304.15, which the Board considers to be inadequate, given the condition of the buildings.

71. Management stated that in 2010, the Agency had allocated $1 million to maintain the most critical buildings, as identified in the assessment of the Infrastructure and Camp Improvement Department.

72. **UNRWA agreed with the Board's recommendation that it: (a) continue to mobilize resources to prevent buildings in bad condition from further deteriorating; (b) prepare a comprehensive long-term asset management plan for its buildings in need of repair, as identified in the valuation report; and (c) develop an asset repair and maintenance policy.**

Inspection report on property, plant and equipment

73. Our review of asset records at the Jordan field office as of November 2012 noted the following deficiencies in property inspection activities:

(a) The forms recording property inspections showed that only 23 (3.3 per cent) of the total of 696 building units/installations had been inspected. Section 2.5.1 of the Property Management Manual requires the inspection of all property, plant and equipment, while section 2.5.5 requires inspected property to be supported by a report on the findings of the inspection. The noted inspections did not include all assets, nor were they supported by a report;

(b) There was no inspection plan to show the timetable for inspections and the necessary resource requirements;

(c) Inadequate inspection of property, plant and equipment may indicate that property, plant and equipment values in the financial statements are not sufficiently or reliably estimated.

74. **UNRWA agreed with the Board's recommendation that it: (a) assign specific officers responsibility for inspecting property and issue a directive to prepare and maintain reports for all inspections undertaken; and (b) prepare an inspection plan for approval by the responsible Heads of field engineering departments.**

Recognition of property, plant and equipment

75. The Board previously noted that UNRWA had completed its project aimed at documenting and performing valuations of its existing land and buildings through the use of consultants and its own building experts and surveyors. Once the lists had been fully documented, UNRWA had determined the fair value and remaining useful life of the land and buildings on the basis of the detailed information it had obtained. On initial recognition (1 January 2010), the value of land and buildings was $366.05 million, depreciated over the remaining estimated useful life as determined by consultants. The collected data were uploaded into the fixed asset sub-ledger to create a fixed asset register.

76. As part of the progressive implementation of IPSAS, UNRWA decided to “early adopt” International Public Sector Accounting Standard 17 and changed its accounting policy to recognize all assets recorded in its asset register, including land and buildings (now referred to as property, plant and equipment), in the statement of assets and liabilities for the biennium ended 31 December 2011. As reported in the financial statements, the net book value of property, plant and equipment as at 31 December 2011 amounted to $381.5 million.

77. During the period under review, UNRWA capitalized and recorded in its assets register buildings worth $10.17 million and capital work in progress amounting to $4.82 million, which had been omitted from the financial statements for the biennium ended 31 December 2011. The financial statements reported the net book value of property, plant and equipment as at 31 December 2012 to be $437.92 million.

Management of the asset register

78. In comparing the asset register and the general ledger, the Board noted a difference of $5.44 million. The Board also noted that in some cases, despite the fact that UNRWA has automated its assets register in the system, the process of recording assets in the register is delayed, resulting in lack of reconciliation between the two records. However, the Board noted that the respective assets exist.

79. **The Board recommends that UNRWA reconcile the general ledger and the asset register on a regular basis to ensure that the assets reported in the financial statements tally with the asset register.**

Assets occupied without legal documents

80. UNRWA has acquired a number of leased buildings and plots of land for field offices that it operates. According to the information recorded in “lease master sheets”, UNRWA has leased a total of 547 buildings and 693 plots of land from Governments and private owners in Jordan, the Gaza Strip, Lebanon, the West Bank and the Syrian Arab Republic. It was, however, noted by the Board that UNRWA has no lease contracts on 41 occupied buildings and 255 plots of land in Jordan, Lebanon, the Syrian Arab Republic and the Gaza Strip.

81. The Board is of the view that in the absence of formal lease agreements with the respective landlords, UNRWA is exposing itself to the risk of illegitimate rental claims from the landlords. In this regard, the Board notes that of the total of $183.45 million in reported contingent liabilities for commercial contracts, some $0.04 million (0.02 per cent) comprises claims from landlords from whom the Agency rents buildings. Although the amount of rent that the Agency is risking is

insignificant, subject to applicable laws relating to improper possession, UNRWA might be evicted from the properties without adequate preparations for an alternative accommodation.

82. **UNRWA agreed with the Board's recommendation that it endeavour to the best of its ability to obtain relevant documents to substantiate the right to use buildings and plots of land.**

10. Inventory management

83. UNRWA recognizes its inventory on delivery and goods in transit only if the risks and rewards shift to the Agency. The inventory balances presented in the financial statements include warehouse inventory, for commodities kept for distribution to refugees; pharmacy/clinics inventory; and production unit inventory (in the Gaza Strip).

Classification of non-inventory items

84. International Public Sector Accounting Standard 12 defines inventory as assets: (a) materials or supplies to be consumed in the production process; and (b) materials or supplies to be consumed or distributed in the rendering of services.

85. The Agency has classified some of its consumable stores, maintenance materials and spare parts for consumption or distribution in the provision of services as "non-inventory items". During our review of IPSAS opening balances, we raised concerns about the lack of clear definitions in the existing inventory policy and recommended a clearer policy on this matter. However, the Board noted that no clear policy has yet been developed for the definition of the two categories of inventory.

86. During our review of inventory stocktaking sheets from main warehouses at the four field offices, we noted that as at 31 December 2012 the Agency had 4,063 items, valued at \$3.38 million, that were classified as non-inventory items. This amount included items with a value of \$0.542 million that qualified as inventory under Standard 12.

87. UNRWA agreed that in future, all inventories as defined in Standard 12 would be counted and reported in the balance sheet at year-end. Furthermore, the Board was informed that currently, the Agency's information technology systems could not capture non-inventory items and that this particular deficiency would be addressed in 2014 through the introduction of the new enterprise resource planning system.

88. **The Board recommends that UNRWA: (a) expedite the process of developing the inventory policy in order to enhance IPSAS compliance; and (b) assess the closing value for non-inventory items to ensure compliance with International Public Sector Accounting Standard 12.**

11. Cash and treasury management

Lack of a structured Investment Review Committee, an up-to-date list of rated banks and a hedging policy

89. Our review of treasury operations for the seven months ended 31 July 2012 noted that UNRWA had invested a sum of \$542.8 million from its four field offices in short-term deposits. The investments were in various currencies and held at

various commercial banks. The investments had earned interest of $0.89 million over the seven-month period. However, the following deficiencies were noted in the investment activity operations:

(a) Upon receiving the Board's request for the minutes of the Investment Review Committee, management informed the Board that there were no formal meetings of the Committee, but rather informal consultations, discussions and approval. Formal Investment Review Committee meetings are a requirement set out in treasury technical instruction No. 3;

(b) There was no hedging policy or strategy for preserving the value of UNRWA resources, as required in paragraph 2.3.2 of the Finance Manual of March 2010 and the technical instruction of 2005. A hedging policy and strategy are an important aspect of the management of currency risks.

90. Management stated that it would introduce a hedging policy, to be approved by the Investment Review Committee.

91. **UNRWA agreed with the Board's recommendation that it: (a) establish a structured Investment Review Committee and ensure that its proceedings are recorded and maintained; and (b) expedite the development of a hedging policy and strategy to guide the treasurer on hedging and the proper management of currency risks.**

12. Results-based management

Lack of a results-based management policy

92. Results-based management is a management approach aimed at changing the way in which an entity operates, with the improvement of performance and the achievement of results as the central focus. The objective of results-based management is to improve the effectiveness and accountability of management by defining realistic expected results and monitoring progress towards their achievement more efficiently.

93. UNRWA develops biennial implementation plans in accordance with its medium-term strategy for 2010-2015, which provides direction and milestones for the headquarters and field office plans. The plans for 2010-2011, 2012-2013 and 2014-2015 under the medium-term strategy contain the logical framework for the programme, with budget indicators and corresponding targets to be achieved during the period to ensure the effective and efficient delivery of services to Palestine refugees.

94. The Board notes that UNRWA introduced a process and guidelines whereby progress made in the implementation of plans is subjected to annual reviews, and that the review of the results for the biennium 2010-2011 were conducted in 2012. The Board notes that despite the establishment of the guidelines, there is no policy or organizational directive to ensure the compliance and accountability of integral results-based management practices in UNRWA. A policy or organizational directive would, in the Board's view, give headquarters more assurance of compliance within the organizational hierarchy and of the achievement of the intended results.

95. The Board analysed the 2012 results collected in the results-based management system and noted that indicators comprising the common monitoring matrix across UNRWA were well defined. However, the Board notes that the

submitted information did not contain data from the Syrian Arab Republic field office, thus limiting the Agency's ability to evaluate the level of compliance of that field office. The Board was informed that the Agency had been unable to collect data from the Syrian Arab Republic field office as a result of the ongoing civil war.

96. **UNRWA agreed with the Board's recommendation that it: (a) formalize its results-based management results review processes in a policy or organizational directive; (b) ensure that the results review process takes place as envisaged, at mid-year and on an annual basis; and (c) ensure that measures are implemented to support alternative means of collecting performance data from the Syrian Arab Republic field office, for example, though the Internet.**

97. UNRWA informed the Board of current developments with respect to the formalization of the results-based management methodology and formulation of organizational directives and that the semi-annual and annual review of results had been put in place in 2013. Moreover, UNRWA explained that with regard to the Syrian Arab Republic field office, a dedicated Report Officer and a Programme Analyst had been hired to support data collection and reporting efforts.

13. Information technology

98. The Board reviewed UNRWA information and communications technology (ICT) governance. The Agency has a Chief, Information Systems Division. The Chief reports to the Director of Administration and Human Resources. The Board notes that UNRWA does not have a permanent ICT steering committee, but has established a steering committee to oversee the implementation and governance of the ongoing enterprise resource planning project. In the absence of an information and communications technology steering committee, the Agency is exposed to a risk of low-quality ICT services and increased costs in delivering ICT services. The Board considers that an ICT steering committee would complement the governance of ICT in ensuring that human and other ICT resources are utilized effectively and efficiently, including through the oversight of strategic information technology solutions.

99. The Agency's ICT support functions are not grouped under one unit. For example, the Finance Department and the Information Systems Division have identical posts: the Department has four posts of Analysts/Programmer, one post of Payroll Administrator and one post of Help Desk Coordinator, to support RAMCO applications, and the Division has the same posts. The Board is of the view that the duplication of common services increases costs and the complexity of managing application support functions and may cause confusion for the recipients of the services provided.

100. The Board also noted that UNRWA does not have a document management system to serve as a central repository accessible from all its offices, located in Jordan, the Gaza Strip, Lebanon, the Syrian Arab Republic and the West Bank. Consequently, during outbreaks of violence or political instability in the region, the flow of information is easily disrupted.

101. **UNRWA agreed with the Board's recommendation that it: (a) set a time frame for establishing an ICT steering committee to oversee the implementation and operation of ICT-related functions; (b) develop a business case for deploying an electronic document management system that will act as a key central**

repository accessible anywhere and at any time; and (c) set a time frame for and expedite the merging of the RAMCO application support unit under the Finance Department with the application support unit under the Information Systems Division.

14. Department of Internal Oversight Services

Internal audit coverage

102. The Board notes that the internal audit department had planned to perform 20 audit assignments during the year but had managed to complete only 2 (10 per cent), together with 4 assignments that had been carried forward from the previous biennium. Also, the Board found that, of the current audits, 2 were at the reporting stage, 3 (15 per cent) were still at the field work stage, 11 (55 per cent) were at the planning stage and 2 (10 per cent) had been stopped.

103. The Board was informed that one of these assignments, relating to staff entitlements and leave management, had been stopped during its preliminary stage owing to the fact that this was considered a low-risk area, while the other, related to security and safety, had been postponed after discussion with the client.

Audit of the Area Staff Provident Fund

104. The Board notes that paragraph 47 of the general provision of UNRWA organizational directive No. 28 (2010) requires that the Department of Internal Oversight Services audit the accounts and operations of the business operations of the Area Staff Provident Fund. However, in 2012 the Department of Internal Oversight Services did not perform any audit activity with respect to the Fund's operations. The Board was informed that the Department had conducted an audit of the Fund in 2008 (the relevant report was issued in 2009) and that the overall opinion had been satisfactory. The Department uses a risk-based approach in selecting audit engagements, and the Fund will be assessed again in October 2013.

105. The Board acknowledges the initiative taken by the Department of Internal Oversight Services to incorporate the Provident Fund into its workplan for 2014, but it is of the view that the Fund needs priority consideration in the Department's annual plan owing to the nature and the volatility of its operation.

Follow-up on internal audit recommendations

106. The Board notes that the report of the Department of Internal Oversight Services for the year ended 31 December 2012, which was submitted to the Advisory Committee on Internal Oversight, disclosed that from January 2010 to December 2012 the Department had issued 42 reports containing a total of 627 recommendations. As of December 2012, the Administration had fully implemented 342 (55 per cent) of all recommendations (see table II.2).

Table II.2
Status of implementation of recommendations of the Department of Internal Oversight Services

Status	*2010*	*2011*	*2012*	***Total***
Not implemented	41 (13%)	89 (49%)	96 (67%)	**226 (36%)**
Partially implemented	50 (17%)	7 (4%)	2 (1%)	**59 (9%)**
Fully implemented	211 (70%)	86 (47%)	45 (32%)	**342 (55%)**
Total	**302 (100%)**	**182 (100%)**	**143 (100%)**	**627 (100%)**

Source: Department of Internal Oversight Services annual report 2012.

107. In its previous report, the Board raised concerns about the slow rate of implementation of internal audit recommendations. The Board, however, notes a significant improvement in the implementation of internal audit recommendations during the year. Of the 235 recommendations ranked as high-risk, 202 (86 per cent) were implemented, leaving a balance of 33 (14 per cent) as of December 2012 (see table II.3). The Board, while acknowledging the good progress made, encourages UNRWA to further reduce the level of outstanding high-risk recommendations.

Table II.3
Summary of outstanding high-risk recommendations, 2010-2012

Year	*High-risk recommendations*	*Implemented*	*Outstanding*
2010	115	99 (86%)	16 (14%)
2011	66	66 (100%)	0 (0%)
2012	54	37 (69%)	17 (31%)
Total	**235**	**202**	**33 (14%)**

Source: Department of Internal Oversight Services annual report 2012.

15. Microfinance Department

108. The Microfinance Department is a small programme within UNRWA that provides credit facilities to micro-entrepreneurs. Activities and balances of the Department for 2012 are included in the financial statements of the Agency for the year ended 31 December 2012. In addition, the Department prepares its own set of financial statements, on which the Board performs a separate audit. The Board audited the Department's 2012 annual financial statements and issued an unqualified opinion, but highlighted the following issues.

Losses due to loan provisioning and devaluation of the Syrian pound

109. The Board noted that as at 31 December 2012, the Agency's Syrian operations had a loss of $3.64 million, with operational self-sufficiency of 29.5 per cent, impeding the Agency's ability to cover running costs. The operational self-sufficiency percentage is a measure of loan portfolio quality, calculated by including interest and recovery as part of operational expenses and additional provisions for loan losses. It measures how well the Department covers its costs through its operating activities.

Management of loans receivable

110. The Board notes that a total of $36.43 million in loans were issued during the year, with respect to which $37.12 million has been repaid. The repaid amount includes part of the previous-year balance of $22.81 million. During the year, the Microfinance Department made a provision of $1.99 million and a write-off of $0.84 million. The closing loan balance as at 31 December 2012 was $20.13 million. In its previous report, the Board noted a lack of implementation of recommendations of internal auditors regarding weaknesses in the granting of loans that might increase the risk of recoverability. The Board notes similar weaknesses, including inadequate follow-up on late and delinquent clients by branch officials, and credit decisions made without background checks as to the integrity and reputation of clients.

Implementation of new loan management information system

111. In its previous audit, the Board noted weaknesses in the general controls over the loan management system that exposed the Microfinance Department to the risk of unauthorized transactions and data integrity. The Board reviewed the information technology general controls and noted similar weaknesses that continue to expose the Department to increased risks of unauthorized transactions and compromised data integrity. Departmental management is installing a new loan management system intended to overcome the system's weaknesses and expects to have achieved complete rollout by August 2013.

112. **UNRWA agreed with the Board's recommendation that it: (a) continue monitoring the loan portfolio in the Syrian Arab Republic with a view to improving its operational self-sufficiency to a level that will enable it to cover its operational costs; (b) improve controls by establishing a loan review committee for the management of loans receivable; and (c) ensure that the general controls of the loan management information system are adequate for the mitigation of ever-growing business risks.**

113. UNRWA informed the Board that it had already begun to implement the recommendation and had also taken several actions to mitigate the risks. In its next audit, the Board will follow up on the progress made.

D. Disclosures by management

1. Write-off of losses of cash, receivables and property

114. UNRWA informed the Board that in accordance with financial regulation 11.5, the following losses and write-offs had been recognized: cash losses of $501 (2010-2011: $30,189), inventory losses of $123,562 (2010-2011: $6.73 million), outstanding receivables of $525,586 (2010-2011: $923,320) and outstanding pledges of $455,243 (2010-2011: $137,553).

2. Ex gratia payments

115. As required under financial regulation 11.5, UNRWA reported ex gratia payments for the period under review amounting to $9,874.09, related to the settlement of treatment and medication fees related to vehicle accidents, and $32,485.88, in respect of a legal settlement for release and discharge, representing a full and final settlement of disputed claims between clients and UNRWA.

3. Cases of fraud and presumptive fraud

116. For the year ended 31 December 2012, UNRWA reported 26 cases of fraud and presumptive fraud to the Board, estimated to amount to $33,079, in accordance with article VII of the Financial Regulations and Rules of the United Nations and the related annexure. The cases are described in annex II.

E. Acknowledgement

117. The Board wishes to express its appreciation for the cooperation and assistance extended to its staff by the Commissioner-General and members of his staff, as well as the staff at the Amman headquarters, the Gaza headquarters, the Jordan field office, the Gaza field office, the Lebanon field office and the Syrian Arab Republic field office.

(*Signed*) Amyas **Morse**
Comptroller and Auditor-General of the
United Kingdom of Great Britain and Northern Ireland
Chair of the Board of Auditors

(*Signed*) Ludovick S. L. **Utouh**
Controller and Auditor-General of the United Republic of Tanzania
(Lead Auditor)

(*Signed*) **Liu** Jiayi
Auditor-General of China

30 June 2013

Annex I

Review of the status of implementation of recommendations for the year ended 31 December 2011

	Summary of recommendation	*Paragraph reference (A/67/5/Add.3, chap. II)*	*Financial period in which first made*	*Implemented*	*Under implementation*	*Not implemented*	*Overtaken by events*
1	Review the adequacy of its long-term resource mobilization strategy to address the cash flows	26	2010-2011	X			
2	Implement adequate strategies to address the residual matters identified in relation to its IPSAS implementation plan	36	2010-2011	X			
3	Develop and implement strategies to enable the organization to fully benefit from IPSAS implementation and assign responsibility for tracking of progress	40	2010-2011	X			
4	Strengthen its controls regarding the preparation and review of its financial statements	44	2008-2009		X		
5	Develop and implement an age analysis for outstanding contributions, and consider the feasibility of including contributions receivable in its accounts receivable module in the general ledger	47	2010-2011	X			
6	Assess the recoverability of long-outstanding value-added tax receivable balances, develop a policy for provision for doubtful debts, and raise a provision for doubtful debts where applicable to accurately reflect its outstanding receivables	51	2010-2011	X			
7	Develop a funding strategy to enable it to honour all its end-of-service liabilities	55	2010-2011		X		
8	Set organization-wide baselines and targets to benchmark its performance, and develop and implement procedures to review the accuracy and completeness of information captured in its performance management system	58	2010-2011	X			
9	Prepare monthly reconciliations for all bank accounts and ensure that they are reviewed by senior officers throughout the financial period	61	2010-2011	X			

	Summary of recommendation	Paragraph reference (A/67/5/Add.3, chap. II)	Financial period in which first made	Implemented	Under implementation	Not implemented	Overtaken by events
10	Avoid implementing projects before the funds have been received from the donors and negotiate with its donors to receive funds in advance for project implementation, in order to reduce the risk involved in implementing projects before advances are received, and put controls in place to ensure quicker clearing of completed projects' fund balances to avoid delays in project closure	66	2010-2011	X			
11	Implement streamlined project monitoring tools to enable its project managers to monitor the implementation of projects at headquarters and in the field	73	2010-2011		X		
12	Close all operationally closed projects in the finance system in a timely manner, and maintain updated financial reports on a monthly basis to avoid delays in project closure	77	2010-2011	X			
13	Allow for adequate tender submission time frames in accordance with the Procurement Manual, provide clarity on what constitutes "due cause", and instruct field offices to institute adequate procurement planning	82	2010-2011		X		
14	Implement adequate reviews of waivers to ensure that proper procurement guidelines and processes are adhered to by all divisions and that waivers are granted only for genuine cases of exigency	90	2010-2011		X		
15	Conduct a review to establish the reasons for the high rate of waivers, implement processes to monitor the use of waivers, and adequately document and justify the use of waivers	92	2010-2011	X			
16	Enforce compliance with procurement procedures	95	2010-2011		X		
17	Prepare and issue comprehensive inventory count procedures to guide and direct the inventory count at field offices	117	2010-2011	X			
18	Enhance its supply manual to address the inconsistent procedures applied by its field offices in issuing inventories and to address the gaps identified in the process of issuing inventories	118	2010-2011		X		
19	Fully implement its human resources strategy and plan	122	2008-2009	X			
20	Implement a process for managing and monitoring vacancies to ensure that critical posts are filled in a timely fashion so that the Agency can deliver services to the refugees	123	2004-2005	X			

	Summary of recommendation	Paragraph reference (A/67/5/Add.3, chap. II)	Financial period in which first made	Implemented	Under implementation	Not implemented	Overtaken by events
21	Expedite the implementation of its performance management policy to ensure that roles and responsibilities are clarified, consequences for non-compliance are specified and appropriate measures are taken against supervisors who fail to comply	130	2010-2011	X			
22	Implement a process for managing vacancies to ensure that adequate time was given for the recruitment of skilled and experienced staff and that the recruitment process remained fair and competitive	133	2010-2011	X			
23	Address the weaknesses identified in the findings of the Department of Internal Oversight Services	134	2010-2011	X			
24	Expedite the process of implementing the monitoring tool for risk management	140	2010-2011	X			
25	Address the weaknesses identified with regard to its security settings and segregation of duties in the information technology functions	143	2008-2009	X			
26	Develop, approve and implement a detailed user account management policy and procedure for application in the management of user access, and regularly review the appropriateness of access rights granted to users	146	2004-2005	X			
27	Assign an additional staff member in the interim to monitor and review all changes made to the system, regularly monitor the activities of the database administrators, and implement an automated logging tool to log all changes made to the system	151	2008-2009	X			
28	Develop a comprehensive physical access and environmental control policy and procedure to be applied to its server rooms	153	2008-2009	X			
29	Clearly define the responsibility for plan testing and process backlog initiation in its disaster recovery plan, finalize and approve the plan, and develop and approve a business continuity plan	158	2002-2003		X		
30	Implement safeguards to ensure that off-site and on-site backup tapes, as well as tapes in transit, are adequately protected from unauthorized physical access and environmental hazards, and formally document all off-site backup arrangements	162	2006-2007	X			
31	Align the organizational directives relating to the Advisory Committee on Internal Oversight with best practice	167	2010-2011	X			

	Summary of recommendation	*Paragraph reference (A/67/5/Add.3, chap. II)*	*Financial period in which first made*	*Implemented*	*Under implementation*	*Not implemented*	*Overtaken by events*
32	Develop plans to expedite the process of recruiting the Director of Internal Oversight Services	171	2010-2011		X		
33	Prioritize the implementation of internal audit recommendations, with emphasis on high-risk areas identified by internal audit	178	2010-2011		X		
34	The Department of Internal Oversight Services should implement the recommendations made by the Institute of Internal Audit	181	2010-2011	X			
35	Review the adequacy of the staff resources and capacity of the evaluation and investigation units and provide the necessary resources	185	2010-2011	X			
36	Consider the implications of the information generated regarding all cases of misconduct in terms of the capacity of the investigation department and the appropriate disposition of cases and the improvement of controls, systems and other fraud prevention measures	188	2008-2009	X			
	Total	**100**		**26**	**10**	**–**	**–**
	Percentage share of total			**72**	**28**	**0**	**0**

Annex II

Cases of fraud and presumptive fraud reported to the Board

Case number	*Office*	*Responsible officer*	*Type*	*Loss (United States dollars)*	*Description*
12-0070	Lebanon field office	Ann Dismorr, Director	General fraud	0	An investigation was carried out into allegations regarding the failure of an education staff member to comply with his obligations, under staff rule 101.4, to declare and obtain permission to engage in outside activities, and to refrain from being actively associated with the management of, or from holding a financial interest in, any business concern where it was possible for him to benefit from such association or financial interest by reason of his position in the Agency.
12-0074	Lebanon field office	Ann Dismorr, Director	General fraud	0	An Outreach Officer in the Employment Unit was arrested by the Lebanese Authority for forging his educational qualifications. The Outreach Officer had earlier tried to apply for a job with a Lebanese governmental body, and his forged documents were discovered as a result.
12-0078	Lebanon field office	Ann Dismorr, Director	General fraud	0	The Front Office received information alleging that on 27 April 2012, during the administration of the recruitment exercise for teachers at a local school, attempts had been made by UNRWA staff to provide unfair advantage to more than one candidate. The Front Office launched an investigation into the matter. The investigation also looked into allegations that one or more staff members had misused their position(s) of authority to coerce and influence other staff to engage in the above-mentioned prohibited conduct.
12-0103	Gaza field office	Robert Turner, Director	Entitlement fraud	79	Case involving the fraudulent claiming of benefits by the family members of a deceased person.
12-0021	Gaza field office	Robert Turner, Director	Financial irregularity	0	Two complaints were received from contractors. The first contractor claimed that members of the youth activity centre had told him that they could secure a job for him provided that the salary was divided among them: they would take 900 new sheqalim, and he would take 500 new sheqalim.
12-0121	Gaza field office	Robert Turner, Director	General fraud	0	In a complaint from staff member X against staff member Y, X claimed that in 2010, Y had taken construction materials from X on the understanding that he would pay for them over time. The cost was 70,000 new sheqalim. Y had sold the materials on the market, and X had asked him for repayment several times, but Y had refused to pay. A document signed by Y was before the court in this regard.
12-0153	Jordan field office	Marta Colburn, Director	Financial irregularity	0	In a cross-complaint related to investigation 12-96, Ms. X alleged that Head Teacher Ms. Y had committed financial and administrative violations. Specifically, unauthorized purchases had been made, and the Head Teacher had paid sales tax on an item while knowing that it was not necessary.

Case number	*Office*	*Responsible officer*	*Type*	*Loss (United States dollars)*	*Description*
12-0254	Jordan field office	Marta Colburn, Director	Financial irregularity	0	An allegation of financial irregularity was raised against Ms. Y, to the effect that she had violated cash receipt procedures by accepting cash from clients and reimbursing the cash payments to the branch cashier. In violation of Microfinance Department cash receipt procedures, allegedly Ms. Y retained the cash received from clients for up to six days prior to reimbursing it to the branch cashier and deliberately manipulated the receipt and reimbursement dates.
12-0046	Jordan field office	Marta Colburn, Director	General fraud	0	Mr. X submitted a complaint, through the Ethics Office, against his supervisors for irregularities in filling out his last periodic evaluation report, claiming that the report had been signed by someone other than him, and that the meeting to discuss the periodic evaluation report, as recorded in the report, had never taken place. Mr. X also provided the last three periodic reports (2009, 2010 and 2011) to substantiate his claims, confirming that the signature on the 2009 and 2010 reports was his own.
12-0172	Jordan field office	Marta Colburn, Director	General fraud	0	The Field Legal Officer received an anonymous complaint alleging that Mr. Y had abused his power and replaced the name of a teacher selected by the board with his sister’s name.
12-0277	Jordan field office	Marta Colburn, Director	General fraud	0	It was reported that members of the area staff union executive committee had complained that they had no information in relation to the circular issued by the Chair of the committee, who had not consulted them in this regard, and that they held the Chair fully responsible for the circular and for issuing it on behalf of the committee.
11-0244	Amman headquarters/ Department of Internal Oversight Services	Michael Kingsley-Nyinah, Director, Syrian Arab Republic field office	Procurement irregularities	0	It was alleged that fraud and corruption had taken place during the construction of the Neirab rehabilitation project, near Aleppo, Syrian Arab Republic.
12-0032	Amman headquarters/ Department of Internal Oversight Services	Felipe Sanchez, Director, West Bank field office	General fraud	0	The allegation refers to procurement irregularities, medical insurance fraud and mismanagement. Specifically, it is alleged that Ms. X, at a local hospital, was involved in misconduct in respect of (a) apparent discrepancies in food purchases at the hospital between September and October 2011, (b) an apparent unpaid debt owed to a pharmacy, and (c) an alleged medical insurance claims fraud.
12-0036	Amman headquarters/ Department of Internal Oversight Services	Marta Colburn, Director, Jordan field office	Procurement irregularities	0	In an anonymous fax message to the Commissioner-General dated 11 March 2012 containing allegations of impropriety relating to the Jordan field office, the author alleged that there had been Xerox contract discrepancies, recruitment irregularities and provision of misinformation to the Director of UNRWA Operations by Mr. Y.

Case number	Office	Responsible officer	Type	Loss (United States dollars)	Description
12-0059	Amman headquarters/ Department of Internal Oversight Services	Marta Colburn, Director, Jordan field office	Procurement irregularities	0	Mr. X informed the Director of the Department of Internal Oversight Services on 28 April 2010 that a vendor had visited the Jordan field office and informed Mr. Y that Mr. Z had solicited a bribe. The solicitation was recorded on camera by the vendor.
12-0118	Amman headquarters/ Department of Internal Oversight Services	Marta Colburn, Director, Jordan field office	Procurement irregularities	0	Allegations were raised that Mr. Y had solicited a bribe together with Mr. Z.
12-0256	Amman headquarters/ Department of Internal Oversight Services	Felipe Sanchez, Director, West Bank field office	General fraud — West Bank cashier's office	33 000	Mr. X called Ms. Maxine Manditsch on 8 October 2012 concerning a fraud in the cashier's office. One case was established in which an international staff member had not received a payment of $700. The Finance Officer found that the payment documents had been stamped as paid but the signature was false. The documents were misfiled, and this was considered highly unusual. The West Bank field office decided to write off the sum and concluded that it would cost too much to investigate the case.
12-0266	Amman headquarters/ Department of Internal Oversight Services	Marta Colburn, Director, Jordan field office	Procurement irregularities	0	28 April 2012, Mr. X informed Mr. Claus Andreasen, Director of the Department of Internal Oversight Services, that a vendor had visited the Jordan field office and informed Mr. Y that Mr. Z had solicited bribes. The solicitation was recorded on camera by the vendor. The vendor was subsequently identified.
11-0235	West Bank field office	Felipe Sanchez, Director	Entitlement fraud	0	Staff member submitted a falsified sick-leave request for 4-17 May 2011.
12-0242	West Bank field office	Felipe Sanchez, Director	Financial irregularity	0	Staff member made ex gratia payments to Procurement and Logistics Division staff.
11-0273	West Bank field office	Felipe Sanchez, Director	Financial irregularity	0	Staff member made a claim for payment of $768, initially submitted to headquarters, and the West Bank field office was instructed to pay the amount to her. West Bank field office records indicated that the payment had been made; however, staff member claimed that she had never received the payment.
12-0132	West Bank field office	Felipe Sanchez, Director	Financial irregularity	0	Allegations were raised regarding discrepancies between actual food purchases at a local hospital and the monthly reports/invoices for September and October 2011, which reflected higher quantities of certain products than those actually received and, if paid, would have resulted in the Agency paying for more than had actually been received.
12-0136	West Bank field office	Felipe Sanchez, Director	General fraud	0	Staff member submitted fraudulent documents that, if processed, would have entitled her mother-in-law to receive health benefits from the Agency. The attempted fraud was discovered before the documents had been processed.

Case number	*Office*	*Responsible officer*	*Type*	*Loss (United States dollars)*	*Description*
11-2072	West Bank field office	Felipe Sanchez, Director	Theft	0	The Shu'fat health centre was robbed overnight.
11-0261	Syrian Arab Republic field office	Michael Kingsley-Nyinah, Director	General fraud	0	The Chief of the Area Office e-mailed the Deputy Director of UNRWA Affairs, the Assistant Director of UNRWA Affairs and the Field Finance Office to inform them that on 4 October 2011, the Area Relief and Social Services Officer, AFA and a driver had left for Latakia with no prior coordination with her and that at 2 p.m. they had called her to inform her that they had finished their work. They asked her to do them a favour by asking the Chief of the Field Relief and Social Services Programme to allow them to spend the night in Latakia. Accordingly, the Chief of the Area Office had called the Administrative Officer of the Programme, who had insisted that no travel subsistence allowance was allowed. The Chief had told them to return. At 4:30 p.m., the Chief had called them, and they had assured her that they were on the way to Homs. However, she had just received a call from her secretary informing her that the three staff members were still in Latakia and that they had obtained permission from the Deputy Director and the Assistant Director, although the security situation was very quiet in Homs.
11-0262	Syrian Arab Republic field office	Michael Kingsley-Nyinah, Director	General fraud	0	The investigators found mistakes in the recording of vouchers and negligence in dealing with financial matters in a community-based organization. They added that this was a common feature in all community-based organizations, not only the community-based organization of Ein El Tal.

Chapter III
Certification of the financial statements

26 March 2013

Pursuant to financial regulations 11.4 and 12.1, I have the honour to submit the consolidated financial statements for the United Nations Relief and Works Agency for Palestine Refugees in the Near East for the year ended 31 December 2012.

I certify that all transactions have been properly recorded in the accounting records and properly reflected in the Agency's financial accounts and appended statements, which I hereby certify as accurate and representative of the Agency's operating activities and the financial state of affairs as at 31 December 2012.

(*Signed*) Shadi **El-Abed**
Officer-in-Charge, Finance Department

Chapter IV
Financial report for the year ended 31 December 2012

A. Introduction

Statement of the Commissioner-General

1. In accordance with regulations 11.2 and 11.4 of the Financial Regulations and Rules of the United Nations Relief and Works Agency for Palestine Refugees in the Near East, I have the honour to submit the consolidated financial statements of UNRWA for the year ended 31 December 2012, which I hereby approve. The financial statements have been prepared and certified as correct by the Director of Finance.

B. Financial and budget analysis

Summary

2. The year 2012 has been a challenging one for UNRWA, its donors and its beneficiaries. The Agency continues to play an essential role in providing vital services for the well-being, human development and protection of more than 5 million registered persons and the amelioration of their plight, pending the just resolution of the question of Palestine refugees. Throughout 2012, UNRWA continued its efforts to meet the needs of Palestine refugees across its five fields of operations despite access problems in the West Bank, the continuing blockade on the Gaza Strip, the outbreak of conflict in the Syrian Arab Republic, and security concerns with which the Agency is faced on a daily basis.

3. Notwithstanding the difficult financial climate, donors continued to provide strong support, with $919.6 million in contributions, allowing UNRWA to continue to provide assistance to beneficiaries and to address emergencies in the Gaza Strip and the Syrian Arab Republic.

4. For the first time, the financial statements of the Agency have been prepared in accordance with IPSAS. Until 2011, the financial statements had been prepared in accordance with the United Nations system accounting standards.

The move to the International Public Sector Accounting Standards

Improved financial reporting and management information

5. On 30 November 2005, the High-level Committee on Management recommended that all United Nations system organizations adopt IPSAS as their accounting standards. This recommendation was driven by a need within the United Nations system to move to improved, independent and universally accepted accounting standards, with the aim of increasing quality and credibility in financial reporting.

6. On 7 July 2006, the General Assembly decided to approve the adoption by the United Nations of IPSAS (see Assembly resolution 60/283, sect. IV, para. 1).

7. Subsequently, the Commissioner-General approved the adoption of IPSAS by UNRWA, and the work of preparing for the implementation of IPSAS commenced in 2009.

8. The adoption of IPSAS represents a best management practice that will keep the Organization up to date with the latest developments in financial matters. It will also lead to greater harmonization in the presentation of financial statements between United Nations system organizations and will improve the comparability of their financial statements with those of other international organizations and national Governments.

9. Financial statements prepared in accordance with IPSAS provide greater insight into the actual assets, liabilities, revenues and expenses of the Agency. Increased transparency with respect to assets and liabilities results in greater internal control and enhanced management of resources. IPSAS-compliant information about revenues and expenses better supports decision-making and enhances strategic planning.

Summary of changes to the financial statements

10. Applying IPSAS requires the introduction of the full accrual basis of accounting, a significant change from the modified cash basis of accounting applied under UNSAS. "Accrual-basis accounting" means the recognition of transactions and events when they occur, recorded in the accounting records and reported in the financial statements for the financial periods to which they relate, and not only when cash or its equivalent is received or paid.

11. Contributions are recognized when confirmed in writing by donors or upon the submission and approval of the required report for subsequent payments in the case of multi-year contracts. Where contributions are due to the Agency, a receivable balance is shown, but this is reduced to reflect an allowance for the amount that is considered unlikely to be received. Previously, under the system accounting standards, revenue from voluntary contributions was simply recognized when cash was received. The Agency now also assesses the value of non-monetary contributions of goods and services in kind, to the extent possible, and includes this in revenue.

12. Expenses are recognized in the financial statements only when services or goods have been received and accepted by the Agency or when goods or services are delivered to UNRWA beneficiaries, not when cash payments have been made.

13. UNRWA now reports the value of its investment in both tangible and intangible assets. Tangible fixed assets (property, plant and equipment) represent the buildings and non-expendable property of the Agency. Intangible assets represent property that does not have physical substance. For the Agency, this is essentially information technology software. Previously, all these assets were immediately recorded as expenditure on acquisition.

14. The value of future employee benefits that UNRWA international and area staff have earned but not yet received (for example, termination liability in the event of the Agency's cessation of operations, accumulated annual leave, repatriation grants) is now recorded on an accrual basis to capture the full cost of employing staff. In the previous financial statements, these types of benefits were shown as an expense only when paid, and the liabilities were disclosed only in the notes.

15. Under the United Nations system accounting standards, the principal financial statements (statements I and II) were presented showing the split by fund. Under IPSAS, only the total consolidated position is shown on the face of financial statements I and II, with the split by fund included in the notes.

16. As permitted under IPSAS, in the first year of IPSAS adoption, comparative information for the prior period has not been provided in the statement of financial performance.

17. The last biennial budget (for 2012-2013) was presented on a modified cash basis. As that basis differs from the accrual basis applied to the financial statements, reconciliation between the budget and the cash flow statement is provided in accordance with the requirements of IPSAS.

Financial performance for 2012

18. The Agency's total revenue and income for 2012 was $944.1 million, compared with total expenses of $991.6 million, resulting in a net deficit of $47.5 million for 2012. The deficit is funded through surplus accrued in previous years.

19. As permitted under IPSAS, in the first year of IPSAS adoption, comparative information for the prior period has not been provided in the statement of financial performance. The financial performance of each fund is detailed in note 32 to the financial statements and is summarized in table IV.I.

Table IV.1
Summary financial performance by fund for the period ended 31 December 2012
(Thousands of United States dollars)

	Unearmarked activities	*Earmarked activities*					
	General Fund	*Restricted funds*	*Microfinance Department*	*Emergency appeals*	*Projects*	*Inter-fund elimination*	***Total***
Total revenues	587.0	32.8	7.7	164.5	174.1	(21.9)	**944.1**
Total expenses	664.0	46.2	10.2	166.7	126.0	(21.5)	**991.6**
Surplus/(deficit) for the year	**(77.0)**	**(13.4)**	**(2.5)**	**(2.2)**	**48.1**	**(0.4)**	**(47.5)**

20. The General Fund, restricted funds, the Microfinance Department and emergency appeals recorded deficits of $77.0 million, $13.4 million, $2.5 million and $2.2 million, respectively.

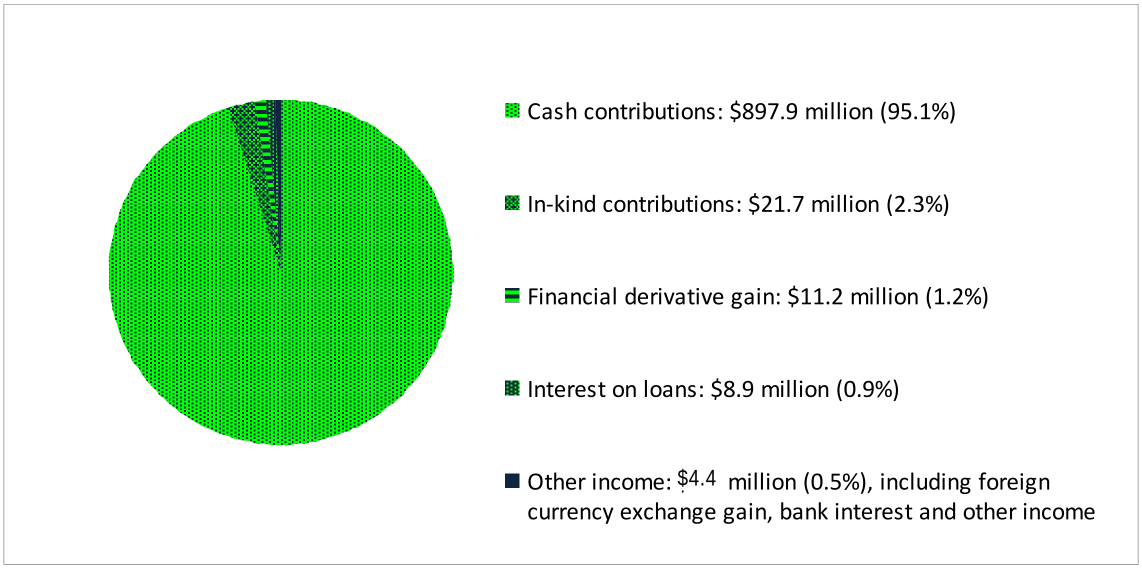
21. The projects fund recorded a surplus of $48.1 million, owing primarily to revenue recognized for projects against which expenses will be incurred in future periods.

Revenue analysis

22. Voluntary cash contributions are the primary source of revenue for the Agency, providing more than 95 per cent ($897.9 million) of total revenue and income. In-kind contributions for earmarked activities (restricted funds, emergency appeals and projects), recognized under IPSAS, were valued at $21.7 million. This is an important element, allowing the Agency to carry out its activities, and includes food

and medical supplies, school textbooks, in-kind services for consultancy and project staff, and the use of land for UNRWA facilities such as schools and health clinics.

Figure I
Revenue and income sources

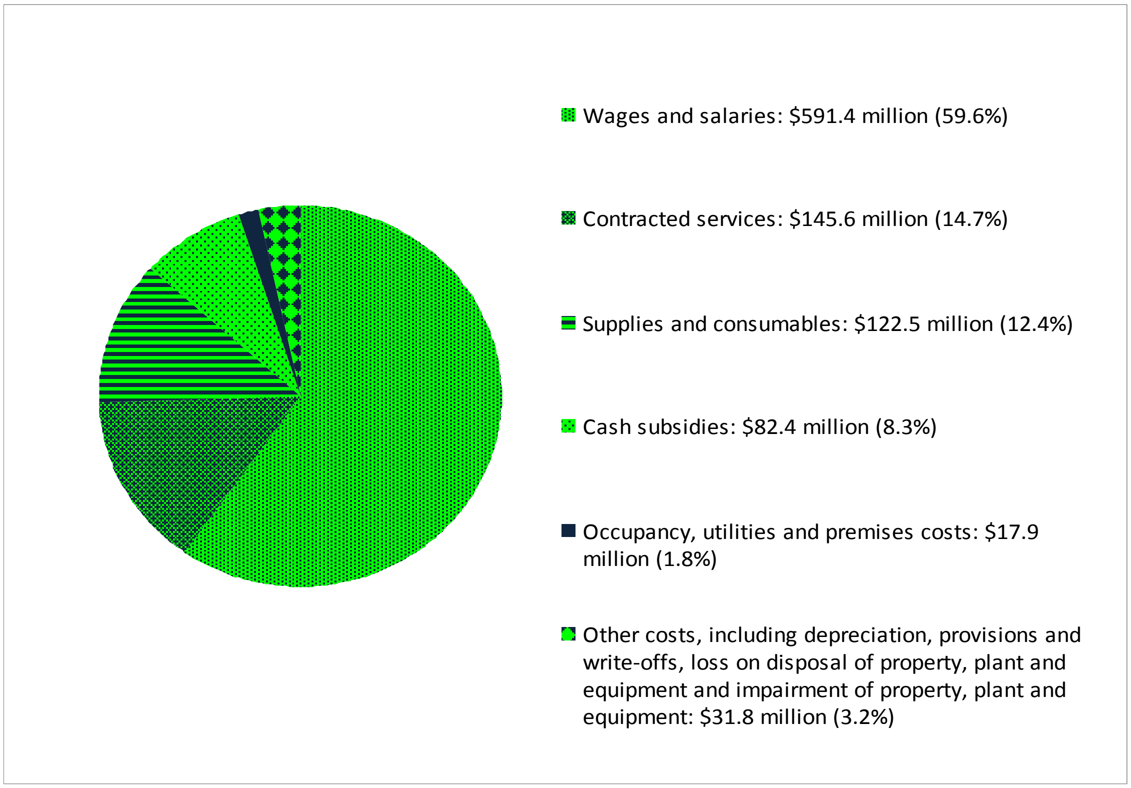


23. All key donors reaffirm their support every six months at a semi-annual Advisory Commission meeting. UNRWA is also actively diversifying its funding base by successfully targeting and increasing donations from emerging markets, such as the Middle East. Furthermore, in 2012 the Agency established a new Partnerships Unit, which has had successful discussions with high-net-worth philanthropic organizations.

Nature of expense analysis

24. UNRWA spent a total of $991.6 million in 2012. Staff costs of $591.4 million represented nearly 60 per cent of total expenses. As already highlighted, accrual accounting for post-employment and other long-term employee benefits requires that the cost of the schemes be recorded as the benefits are earned by staff, rather than on a pay-as-you-go basis. This methodology allows the Agency to better account for the true cost of employing its staff on an annual basis.

Figure II
Expense analysis by nature of expense



25. A total of $145.6 million was spent on contracted services, representing expenses relating to the Agency’s engagement of third parties to perform work on its behalf. Of this amount, $74.2 million was spent on equipment and construction, which includes shelters and equipment that was donated to UNRWA beneficiaries and was therefore expensed, as well as minor equipment for use by the Agency. A total of $18.7 million under the category of contracted services was spent on hospital services for the benefit of refugees.

26. A total of $82.4 million was spent on subsidies, including $61.3 million distributed to beneficiaries providing selective cash assistance for conflict-affected Palestine refugees in the Syrian Arab Republic, food security and rent subsidies. The sum of $14.0 million was provided as subsidies for the construction and repair of shelters, and $4.9 million was provided for patient subsidies.

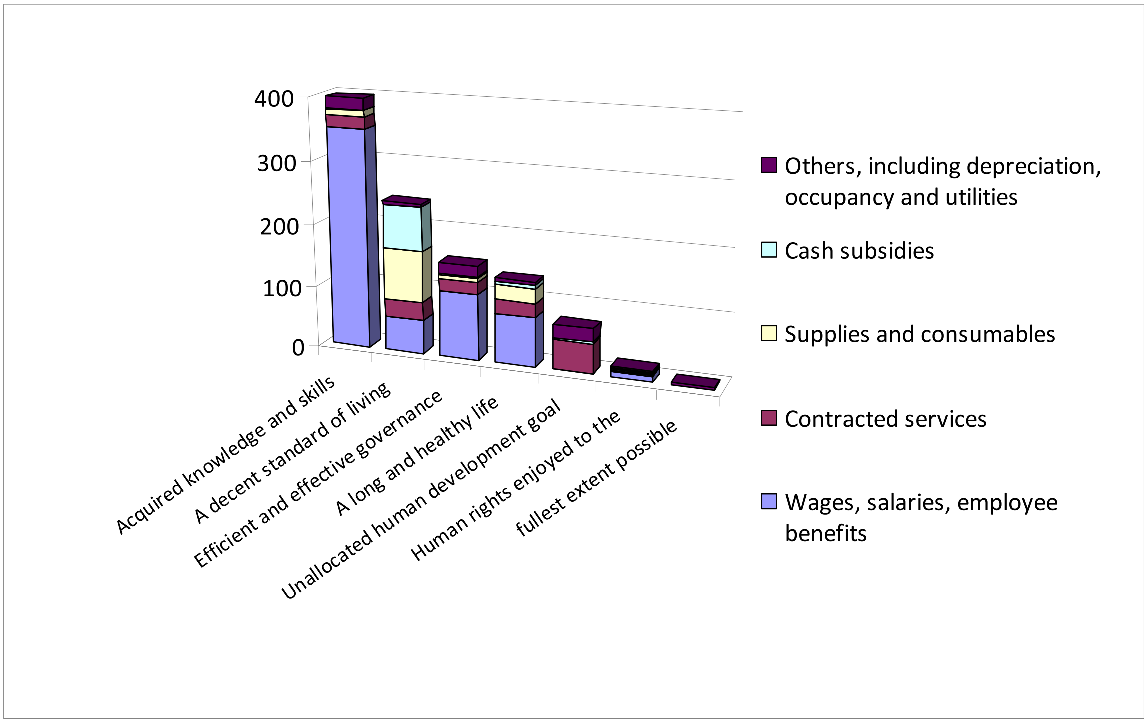
27. A total of $122.5 million was spent on supplies and consumables, including $75.3 million for basic commodities and $1.5 million for fresh food. The amount of $23.3 million was spent on medical supplies, and $5.8 million was spent on text and library books. The sum of $6.3 million was spent on transportation supplies.

28. Occupancy and utility costs totalled $17.9 million in 2012. Other expenses amounted to $31.5 million, including depreciation, impairment of fixed assets and provisions and write-offs.

Human development goals and Agency programmes: expense analysis

29. As part of its planning approach, UNRWA has five human development goals to provide it with direction in fulfilling its mission of helping Palestine refugees. The goals, and the amount spent on each, are shown in figure III.

Figure III
Expense analysis by human development goal[a]
(Millions of United States dollars)

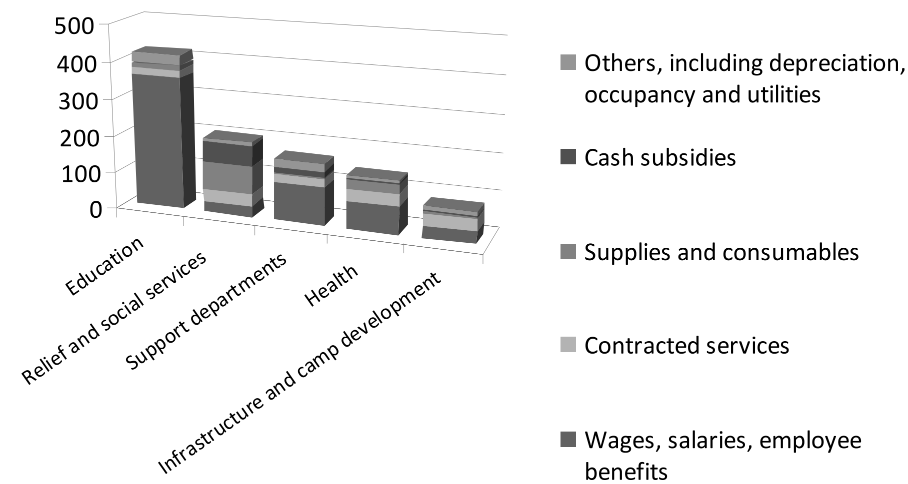


[a] $21.5 million in inter-segment eliminations excluded from analysis.

30. UNRWA is functionally organized under five programmes that provide services to its UNRWA beneficiaries or internal support services. The 2012 expenses by programme, as shown in figure IV, follow a similar expense profile as categorized by human development goal.

31. The largest amount, $396.8 million, representing 40 per cent of the Agency's 2012 expenses, was spent on the goal of "Acquired knowledge and skills" delivered through the education programme ($418.7 million). The "Acquired knowledge and skills" goal is aimed at ensuring universal access to and coverage of basic education, enhancing education quality and outcomes against set standards, and improving access to education opportunities for learners with special education needs. The education programme also provides vocational and technical training and encourages the progression of students to higher education through scholarships. Given the nature of the programme/goal, the vast majority of the expenditure in this area is spent on educational staff wages and salaries.

Figure IV
Expense analysis by programme[a]
(Millions of United States dollars)



[a] $21.5 million in inter-segment eliminations excluded from analysis.

32. An amount of $240.1 million, or 24 per cent of UNRWA expenditure, supported the Human Development Goal of "A decent standard of living", delivered largely through the relief and social services and infrastructure and camp development programmes ($202.7 million and $83.8 million, respectively). The objectives of this goal are to reduce abject poverty, to mitigate the effects of emergencies on individuals, to offer inclusive financial services and increased access to credit and savings facilities, to improve employability, and to improve the urban environment. Thirty-four per cent of the expenditure ($81.9 million) in pursuit of this goal was spent on supplies and consumables, including the provision of food aid for Palestine refugees. An additional $70.5 million was provided in the form of cash subsidies.

33. An amount of $151.4 million, or 15 per cent of the Agency's 2012 expenses, supported the "Effective and efficient governance" goal, accomplished largely through the support departments programme ($164.7 million). The goal is aimed at providing overall direction and control of UNRWA and ensuring efficient operations and effective financial and risk management. The programme includes the effective management of personnel and financial resources, oversight, internal communication, legal support, fundraising, advocacy and outreach to external interlocutors. Sixty-nine per cent of the expenditure in pursuit of this goal ($105.0 million), was spent on wages and salaries.

34. The Human Development Goal of "A long and healthy life" is aimed at ensuring universal access to quality and comprehensive primary health care, protecting and

promoting family health, and preventing and controlling diseases. An amount of $135.3 million (14 per cent of the Agency's total expenditure) was spent in pursuit of this goal, which is supported through the health programme ($143.3 million). Nearly 60 per cent ($79.6 million) of the expenditure in pursuit of this goal was spent on wages and salaries, with 17 per cent ($23.6 million) spent on medical supplies and consumables and 16 per cent ($21.8 million) spent on contracted services to enable Palestine refugees to gain access to health-care services and to support the environmental health subprogramme. An additional 4 per cent ($5.4 million) was spent on cash subsidies to further enable Palestine refugees to gain access to secondary and tertiary health-care services.

35. A total of $72.9 million was spent on projects that have not been assigned to a Human Development Goal, e.g., emergency appeals. Of this amount, 65 per cent ($47.2 million) was spent on contracted services and 30 per cent ($21.6 million) was spent on programme support costs, reflecting the project nature of the unassigned costs.

36. Finally, $16.6 million was spent on the Human Development Goal of "Human rights enjoyed to the fullest extent possible". This includes the objectives of ensuring that service delivery meets the protection needs of beneficiaries, safeguarding and advancing the rights of Palestine refugees, strengthening the capacity of refugees to formulate and implement sustainable social services in their communities, and ensuring that Palestine refugee registration and eligibility for UNRWA services are carried out in accordance with relevant international standards. The services provided for the achievement of these objectives are delivered largely through the relief and social services programme, together with the services provided to achieve the objectives of the Human Development Goal of "A decent standard of living".

Geographical location: expense analysis

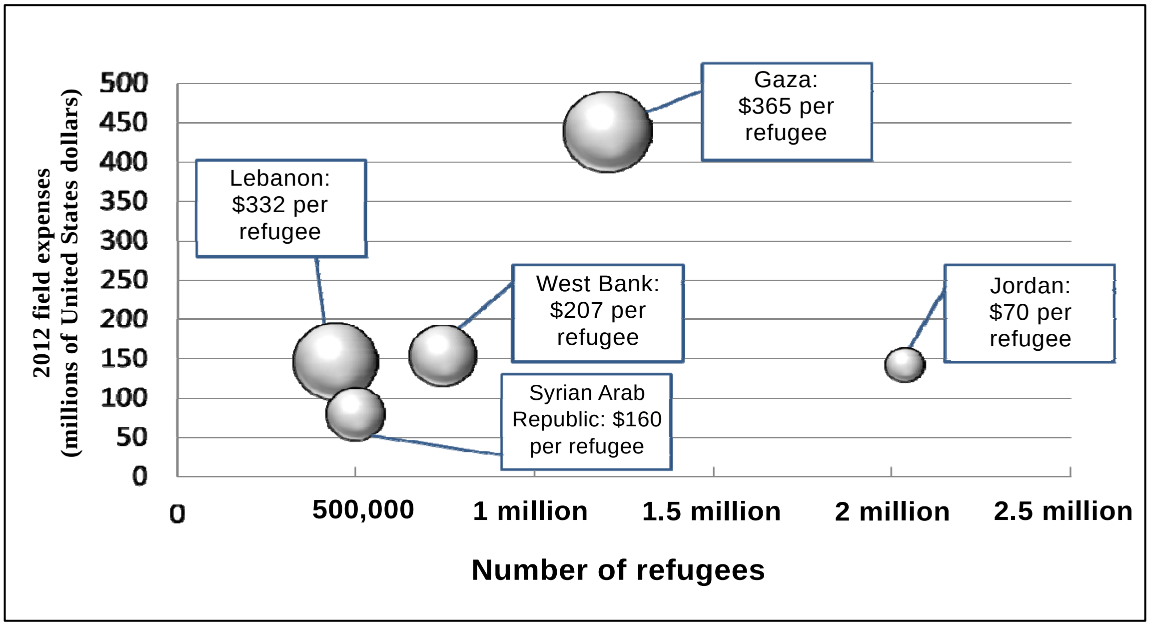
37. Although the Agency's goals and services are delivered primarily within a programme approach, its operations are managed on a field basis. UNRWA operates in five fields: Jordan, Lebanon, the Syrian Arab Republic and the occupied Palestinian territory (the West Bank, including East Jerusalem, and the Gaza Strip). Each field provides similar services, but is distinctive to some extent owing to the particular political, humanitarian and economic contexts in which the field operates and the status and rights of the Palestine refugees enjoyed in it. Figure V shows the costs of UNRWA services per refugee for each field. The different levels of expenditure reflect the situations prevailing in each of the fields.

38. The Gaza field office had the highest average 2012 expenses per refugee, at $365. The Gaza Strip has a population of more than 1.5 million, including some 1.3 million registered Palestine refugees. The ongoing blockade of the Gaza Strip has severely affected the economy and the enjoyment of a range of human rights by Palestine refugees, and this is reflected in the average expenses per refugee in the field. The field office supports eight camps, 243 schools, two vocational and technical training centres, 21 primary health centres, six community rehabilitation centres and seven women's programme centres.

39. The Lebanon field office has the lowest number of registered refugees, at just over 441,500. The relatively high level of average 2012 expenses per refugee, at $332, reflects the conditions prevailing in Lebanon. Palestine refugees do not enjoy several

basic human rights (e.g., they have restricted access to the local labour market), and many live in UNRWA refugee camps. The field office supports 12 camps, 68 schools, two vocational and technical training centres, 28 primary health centres, one community rehabilitation centre and nine women's programme centres.

Figure V
Average 2012 expenses per registered refugee, by field[a]



[a] $52.1 million in headquarters expenses and $21.5 million in inter-segment eliminations excluded from analysis.

40. The West Bank field office serves more than 741,000 registered Palestine refugees, with one quarter of the registered refugees living in 19 refugee camps. West Bank refugees have been hard hit by closures imposed on the West Bank by the Israeli authorities, as historically they have been largely dependent on income from work inside Israel. The average 2012 expenditure per registered refugee in the West Bank was $207. In addition to the 19 camps, the field office supports 98 schools, three vocational and technical training centres, 42 primary health centres, 15 community rehabilitation centres and 16 women's programme centres.

41. The Syrian Arab Republic field office is mandated to provide services to nearly 500,000 Palestine refugees living in the official camps and the three unofficial camps in the Syrian Arab Republic. The average 2012 expenses per registered refugee totalled $160. The ongoing armed conflict in the Syrian Arab Republic has affected the economy, thus impacting the Palestine refugee community. The field office supports nine camps, 118 schools, the Damascus Training Centre, 23 primary health centres, five community rehabilitation centres and five women's programme centres.

42. Finally, more than 2 million Palestine refugees are registered in Jordan. All Palestine refugees in Jordan have full citizenship with the exception of some 140,000 refugees originally from Gaza, who are eligible for temporary passports but are not

entitled to vote or to work in government. The lowest average 2012 expenses per refugee, at $70, reflect the situation of Palestine refugees living in Jordan. The field office supports 10 camps, 172 schools, two vocational and technical training centres, 24 primary health centres, eight community rehabilitation centres and 12 women's programme centres.

Financial position at the end of 2012

43. The Agency's net assets/equity decreased from $282.9 million as at 1 January 2012 (restated in accordance with IPSAS) to $206.6 million as at 31 December 2012.

44. The financial position of each fund is detailed in note 32 to the financial statements and is summarized in table IV.2.

Table IV.2
Summary financial position by fund as at 31 December 2012
(Millions of United States dollars)

	Unearmarked activities	*Earmarked activities*					
	General Fund	*Restricted funds*	*Microfinance Department*	*Emergency appeals*	*Projects*	*Inter-fund elimination*	***Total***
Current assets	90.4	10.5	28.3	40.1	190.4	(0.8)	**358.1**
Non-current assets	400.6	7.6	3.1	2.4	33.9	–	**447.8**
Total assets	**491.0**	**18.1**	**31.4**	**42.5**	**224.3**	**(0.8)**	**806.5**
Current liabilities	121.2	1.9	1.4	9.9	21.1	(0.5)	**155.1**
Non-current liabilities	431.1	0.1	12.1	0.1	1.4	–	**444.8**
Total liabilities	**552.3**	**2.0**	**13.5**	**10.0**	**22.5**	**(0.5)**	**599.9**
Net assets/equity	**(61.3)**	**16.1**	**17.9**	**32.5**	**201.8**	**(0.3)**	**206.6**

45. The negative net assets/equity position of the General Fund is due primarily to the significant post-employment benefits liabilities, recognized for the first time in the financial statements.

46. The net assets/equity balance of the projects fund showed a balance of $201.8 million, due primarily to contributions received or pledged for specific projects against which expenses are expected to be incurred in future years.

47. Net assets/equity are divided into fund balances ($199.5 million) and reserves ($2.3 million).

48. Although there is a negative net current asset balance for the General Fund, the net current assets (current assets less current liabilities) of the Agency were $203.7 million as at 31 December 2012 (compared with $258.3 million as at 1 January 2012), indicating positive short-term liquidity. The Agency's current assets amount to 44 per cent of its total assets, whereas current liabilities constitute 26 per cent of total liabilities.

Cash, cash equivalents and investments

49. Total cash amounted to $232.4 million as at 31 December 2012, covering four to five months of operations (based on average monthly cash outflows in 2012). UNRWA holds no short-term investments.

Receivables

50. Contributions receivable represent confirmed pledges outstanding from donors that are due within 12 months and were valued, net of allowances for estimated reductions in contribution revenue and doubtful accounts, at $22.8 million as at 31 December 2012, owing primarily to projects ($12.0 million) and emergency appeals ($7.6 million).

51. Accounts receivable, net of allowances, were valued at $50.6 million as at 31 December 2012. This relates primarily to significant value-added tax refund claims of $76.6 million, which are still due to the Agency for services and goods procured for the West Bank and the Gaza Strip, as well as $5.3 million related to personal accounts of UNRWA staff members. Loans receivable, net of allowances, were valued at $22.1 million and relate to loans from the Microfinance Department and the microcredit community support programme. Of this amount, $19.4 million relates to short-term (current) loans receivable.

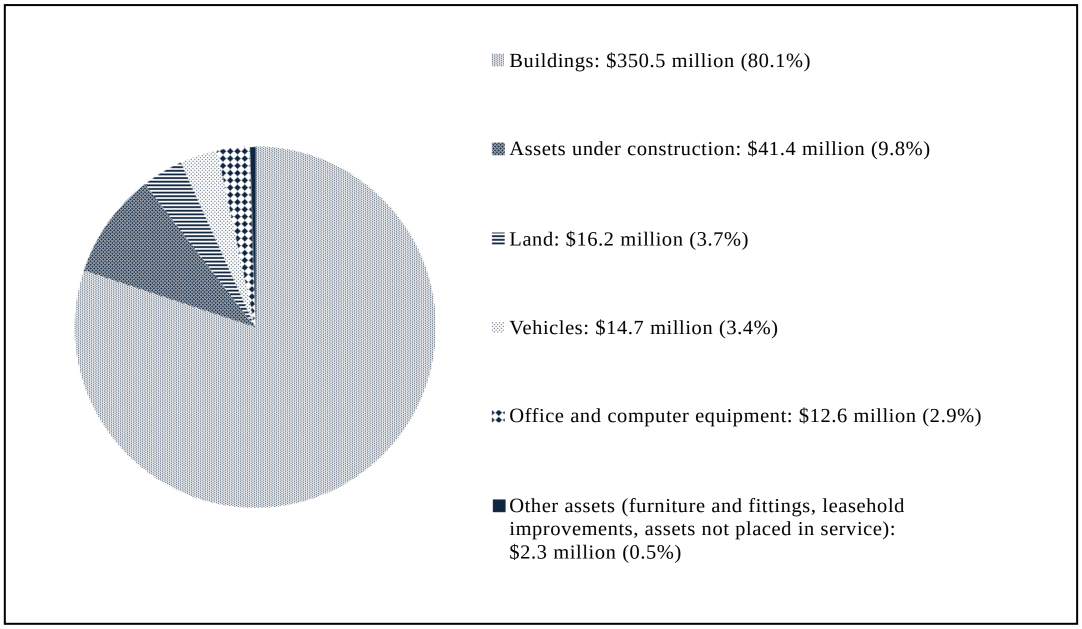
Inventories

52. The value of the Agency's inventory at the end of 2012 was at $29.6 million, reflecting an increase of $1.0 million compared with 1 January 2012 (restated in accordance with IPSAS). This included warehouse inventory of $23.2 million as well as inventory in transit of $2.9 million, consisting of medical supplies, food, motor transport and general supplies to be distributed to Palestine refugees. Pharmacy/health clinic inventory was valued at $3.3 million, and production unit inventory, for the embroidery centre located in the Gaza Strip, was valued at $0.2 million.

Plant, property and equipment

53. The move to IPSAS means that the Agency is now required to maintain detailed records of all property, plant and equipment, which will allow for more rigorous stewardship of assets and matches the charge for the use of assets with services provided. The total net carrying amount as at 31 December 2012 was $437.8 million, representing 54.3 per cent of total Agency assets. This was composed mainly of buildings used for the provision of services to UNRWA beneficiaries.

Figure VI
Property, plant and equipment



54. Assets under construction amounted to $41.4 million as at 31 December 2012, relating largely to specific construction projects under the restricted funds and projects segments. Upon the completion of capital projects using earmarked funds, assets are transferred to the General Fund for use in the delivery of the Agency's core services to Palestine refugees.

55. Land was valued at $16.2 million as at 31 December 2012. This figure seems relatively low, because host Governments and some charitable organizations provide the use of land for no or nominal rent to UNRWA for the benefit of Palestine refugees. The leases under these contracts have been assessed as operating leases, and therefore such land is not included in the UNRWA balance sheet.

Employee benefits liabilities

56. The Agency has significant liabilities relating to post-employment and other long-term employee benefits, amounting to $497.2 million as at the end of 2012, reflecting an increase of $54.5 million during the year. The employee benefits liabilities represent 82.9 per cent of the Agency's liabilities, with $63.6 million categorized as current liabilities and $433.6 million as non-current liabilities. Actuarial valuations have been used for termination and separation costs, employee disability and death-in-service benefits, accumulated annual leave, after-service health insurance and repatriation benefits.

Budgetary analysis

Basis of the budget

57. UNRWA budget figures are determined on a modified cash basis (i.e., United Nations system accounting standards) and disclosed in the statement of comparison

of budget and actual amounts (statement V) as the original budget derived from the 2012-2013 programme budget (Blue Book), as recommended by the Advisory Committee on Administrative and Budgetary Questions and approved by the General Assembly.

58. As compared with the Blue Book budget, the General Fund budget, made available at the beginning of each year, reflects reduced requirements based on the end-of-year income forecast. However, for the projects budget, the resources are made available when contributions are received and/or, on an exceptional basis, when funds are confirmed by donors for approved projects and through advances from the advance financing facility.

59. With the adoption of IPSAS, UNRWA has internally moved from a United Nations system accounting standards budget to an IPSAS budget (accrual budget). Hence, the final budget set out in financial statement V refers to an IPSAS budget and is used for comparison with the actual amounts.

60. The UNRWA budget encompasses three main entities (fund types): the General Fund unearmarked budget, funded mainly by voluntary contributions along with 146 international staff funded through the United Nations regular budget from assessed contributions; General Fund in-kind donations; and the projects budget.

61. The Agency's budget structure follows a results-based budgeting format, as reflected in the two-year field implementation and headquarters department implementation plans, which are derived from the medium-term strategy for the period 2010-2015.

Explanation of material differences

62. Explanations of material differences between the original budget and the final budget as well as between the final budget and the actual amounts are presented below.

Original and final budgets (income and expenses/capital expenditure)

63. The original income of the General Fund budget is the projected income as reflected in the Blue Book, which for 2012 was $521.7 million. As for the General Fund in-kind donations and projects budgets, original income is equivalent to the budgeted figures reflected in the Blue Book on the assumption that all will be funded.

64. The final income of the General Fund budget is the actual income received, while for the General Fund in-kind donations and projects budgets, final income is equivalent to the total budget allocation at year-end.

65. The original budget of expenses/expenditure is the budget as published in the Blue Book, while the final budget of expenses/expenditure is the approved 2012 budget allocation at year-end.

66. The 2012 programme budget, as reflected in the Blue Book for 2012-2013, amounted to $1,013.8 million (United Nations system accounting standards view). This is disclosed in financial statement V as "original budget". In compliance with IPSAS, the final 2012 programme budget (accrual budget) was $1,044.9 million, representing an increase of $31.1 million, or 3.1 per cent. This is disclosed in financial statement V as "final budget". The $31.1 million is a reflection of the increase in the

final budget for each entity as follows: an increase in the General Fund budget by $5.7 million, due to IPSAS changes and reductions in other costs; an increase in the projects budget by $18.2 million, reflecting the additional needs in the Gaza, Lebanon and Syrian Arab Republic field offices; and an increase in General Fund in-kind donations by $7.2 million. The following are the main basic changes as UNRWA moved from the United Nations system accounting standards to IPSAS with respect to the General Fund budget:

$653.1 million	**2012 original budget — General Fund budget**
+$44.9 million	**Severance provision** (recorded monthly as an expense on the statement of financial performance — non-cash item)
+$20.4 million	**Depreciation** (net increase in depreciation of property, plant and equipment)
-$2.7 million	**Capital** (transfer from expenditure to capital expenditure)
-$6.6 million	**Early voluntary retirement** (no longer reported on the statement of financial performance; it is a statement of financial position item)
-$13.1 million	**Retirement benefits** (taken upon retirement; no longer reported on the statement of financial performance; under IPSAS statement of financial position)
-$13.0 million	**Enterprise resource programme** (is capital in nature and an intangible asset; hence, transfer from expenditure to capital expenditure)
-$9.2 million	**Net redeployments — budget hearing results**
$673.8 million	**1 January 2012 IPSAS budget — core General Fund budget**
+$10.3 million	Supplies and consumables (food — redeployment through the year)
+$3.4 million	Cash subsidies — redeployment through the year
-$1.0 million	Contracted services — redeployment through the year
-$0.8 million	Equipment and construction — redeployment through the year
-$39.8 million	**Provision — decrease in end-of-year forecast and redeployment through the year**
$645.9 million	**31 December 2012 IPSAS final budget — General Fund expense budget**
+$12.9 million	**31 December 2012 IPSAS final budget — General Fund capital budget**
+$658.9 million	**31 December 2012 IPSAS final budget — General Fund expense and capital expenditure**
+$377.0 million	**31 December 2012 projects budget**
+$9.0 million	**31 December 2012 in-kind donations budget**
$1,044.9 million	**31 December 2012 total final budget**

Utilization of the budget

67. The variation in the budgetary utilization of the different budget cost components is due to various factors such as salary increase, increase in severance provision (IPSAS adjustment), depreciation provision (IPSAS adjustment), and purchase orders and the relevant hard commitments not reflected in the actual amounts (IPSAS adjustment). The utilization rate against the various cost components rates is outlined below:

- Wages, salaries and employee benefits: 102 per cent, owing to an increase in the severance provision;
- Supplies and consumables: 75 per cent, owing to unliquidated purchase orders;
- Occupancy, utilities and premises costs: 112 per cent, owing to high costs;
- Contracted services: 43 per cent, owing to unliquidated service contracts at year-end;
- Cash subsidies: 75 per cent, owing to timing differences for cash subsidies to be funded from projects;
- Depreciation and amortization: 105 per cent, owing to additional assets capitalized during the year, not included in the budget.

C. Enhancing transparency and accountability

68. Financial regulation 5.2 requires that the Commissioner-General of UNRWA maintain a system of internal controls to provide for an effective current examination or review of financial transactions to ensure the regularity of the receipt, custody and disposal of the resources of the Agency, to ensure the conformity of all expenses with the provisions of the Financial Regulations, and to detect any uneconomic use of the resources of the Agency.

69. The Agency has a system of internal controls that are meant to safeguard assets; ensure adherence to regulations and rules, including management policies and procedures; and prevent fraud. In order to enhance transparency and control and ensure that no single individual has the final say in decisions, most high-level managerial responsibilities and decisions are administered by committees. The Agency has established detailed instructions and procedures to ensure effective financial administration and the exercise of economy. There are also organizational directives to guide the day-to-day running of the Agency and ensure adherence to internal controls.

70. In addition, the Department of Internal Oversight Services regularly reviews the effectiveness of the Agency's system of internal controls and makes recommendations for improvements. Furthermore, the Advisory Committee on Internal Oversight, which is an external expert body, reviews, among other things, the functioning of the system of internal controls and advises the Commissioner-General in this regard. The Committee also reviews the Department's risk-based audit plans and audit work.

71. IPSAS-based financial statements will enhance the transparency of the Agency's financial position and its use of resources. These are the first set of IPSAS-based financial statements prepared by UNRWA, reflecting best accounting

practice, and thereby providing more relevant and useful financial information to UNRWA stakeholders and improving the transparency and accountability of UNRWA in the management of its resources.

72. Furthermore, since 2010, monthly financial reports have been issued to the members of the UNRWA Management Committee and to major donors. This has increased transparency both internally and externally, and the reports to senior management have served to strengthen the focus of senior management on identified financial risks.

D. Enterprise and financial risk management

Enterprise risk management

73. A broad spectrum of risks are associated with the existence and the operations of UNRWA. These risks fall mainly in the broad categories of operational, environmental and financial risks. The management of risks is aimed at reducing the Agency's exposure to various forms of loss and, more critically, to shortcomings in the delivery of services to the Palestine refugees in the areas of education, health, relief and social services, and infrastructure and camp improvement.

74. "Operational risk" refers mainly to the risk of failing to deliver the services for which, according to its mandate, the Agency exists. Such risk is managed through proper planning, control and performance reviews and evaluations in the Agency's main areas of operation (education, health, relief and social services, and infrastructure and camp improvement).

75. Operational risk is also managed at the field level because, although the five fields in which UNRWA operates share similarities, they are also distinctive. In recognition of this, in 2009, responsibility was devolved to the fields for the delivery of services to UNRWA beneficiaries. While guided by the Agency's goals and programmes of priority services, this devolution to operational fields has provided greater discretion to field offices in providing services geared towards local needs, given the realities in the field and within the field's available resources. This devolution, along with centralized policymaking and the regular monitoring of results, provides for enhanced management of the Agency's operational risk.

76. "Environmental risk" is the inherent risk associated with the volatile nature of the environment in which the Agency operates. Such risk is managed through recognition of the potential danger and the political and security concerns posed by the conflicts in the greater Middle East, particularly in the areas where the Agency operates: Jordan, the Syrian Arab Republic, Lebanon, the West Bank and the Gaza Strip. The security alerts are set at the appropriate levels, and all risk-mitigating elements are installed and monitored on an ongoing basis.

Financial risk management

77. The Agency is prone to exposure to various forms of financial risk, the greatest of which is the risk of failure to have sufficient financial resources to achieve the planned objectives and activities. The source of funding for operations aimed at meeting the objectives of the Agency and the needs of the refugees is predominantly the donor community. The uncertainty surrounding the timing and the actual amounts of voluntary contributions also poses some financial risk when it comes to

planning. Such risk is managed in the best way possible by considering the available information and providing for inflows in the most prudent manner.

78. The Agency's activities expose it to a variety of financial risks, primarily the effects of changes in foreign currency exchange rates, as the majority of contributions are in currencies other than the Agency's reporting currency, the United States dollar. As a result, UNRWA financial risk management focuses on the unpredictability of foreign exchange rates and seeks to minimize, where feasible, potential adverse effects on the Agency's financial performance. Financial risk management is carried out by a central treasury function using UNRWA technical guidelines covering areas of financial risk, such as foreign exchange, the use of derivative financial instruments and the investment of excess liquidity. There is no perceived risk that receivables and payables will not be liquidated when they fall due.

79. UNRWA employee benefits liabilities totalled $497.2 million as at 31 December 2012. UNRWA has sought advice from independent actuaries in establishing the value of these liabilities. The funding of employee benefits liabilities remains a long-term risk for the Agency.

E. Responsibility

80. In accordance with regulations 11.2 and 11.4 of the Financial Regulations and Rules of the United Nations Relief and Works Agency for Palestine Refugees in the Near East, I am pleased to submit the following financial statements, which have been prepared under IPSAS. The financial statements have been prepared and certified as correct by the Director of Finance.

Statement I	Financial position as at 31 December 2012
Statement II	Financial performance for the year ended 31 December 2012
Statement III	Changes in net asset/equity for the year ended 31 December 2012
Statement IV	Cash flow for the year ended 31 December 2012
Statement V	Comparison of budget and actual amounts for the year ended 31 December 2012

Notes to the financial statements

(*Signed*) Filippo **Grandi**
Commissioner-General

Chapter V
Financial statements for the year ended 31 December 2012

United Nations Relief and Works Agency for Palestine Refugees in the Near East

Statement I
Financial position as at 31 December 2012
(Thousands of United States dollars)

	Relevant note	*31 December 2012*	*1 January 2012 (restated)*
Assets			
Current assets			
Cash and cash equivalents	4	232 433	270 013
Short-term loans receivable	5	19 421	23 472
Contributions receivable	6	22 801	17 855
Accounts receivable	7	50 555	34 404
Other current assets	8	3 977	4 517
Inventories	9	29 632	28 613
Derivative financial instruments	10	–	20 197
Non-current assets			
Other non-current assets	8	354	–
Long-term loans receivable	5	2 677	1 603
Property, plant and equipment	11	437 772	414 833
Intangible assets	12	6 874	150
Total assets		**806 496**	**815 657**
Liabilities			
Current liabilities			
Payables and accruals	13	62 015	59 932
Employee benefits	14, 15	63 648	60 592
Other current liabilities	16	9 443	3 147
Advance contributions	17	19 998	17 082
Non-current liabilities			
Employee benefits	14, 15	433 571	382 133
Other non-current liabilities	13	11 188	9 875
Total liabilities		**599 863**	**532 761**
Net assets		**206 633**	**282 896**
Net assets/equity			
Other reserves		(11 555)	17 375
Capital reserve: microcredit community support programme and Microfinance Department	19	25 756	25 638
Accumulated surplus/deficit		192 432	239 883
Total net assets/equity		**206 633**	**282 896**

United Nations Relief and Works Agency for Palestine Refugees in the Near East

Statement II
Financial performance for the year ended 31 December 2012
(Thousands of United States dollars)

	Relevant note	*31 December 2012*
Revenue		
Cash contributions	20	897 884
In-kind contributions	21	21 686
Interest on loans	22	8 870
Interest on bank deposits	23	1 155
Other revenue		
Foreign currency exchange gain	24	1 931
Programme support cost recovery	25	167
Financial derivative gain	10	11 232
Miscellaneous revenue	26	1 216
Total revenue		**944 141**
Expenses		
Wages, salaries and employee benefits	27	591 389
Supplies and consumables	28	122 507
Occupancy, utilities and premises costs	29	17 872
Contracted services	30	145 644
Subsidies	31	82 414
Depreciation	11	22 933
Provision and write-offs	5, 6, 7	6 732
Loss on disposal	11	1 422
Impairment of property, plant and equipment	11	679
Total expenses		**991 592**
Surplus/(deficit) for the year		**(47 451)**

United Nations Relief and Works Agency for Palestine Refugees in the Near East

Statement III
Changes in net assets/equity for the year ended 31 December 2012
(Thousands of United States dollars)

		Revaluation reserve	*Other reserve*	*Reserves, microcredit community support programme and Microfinance Department*	*Accumulated surplus/deficit — unearmarked*	*Accumulated surplus/deficit — earmarked*	*Total*
As at 31 December 2011 per United Nations System Accounting Standards	(note 3)	17 375	442 153	25 638	828	118 736	604 730
Reclassification to accumulated surplus			(442 153)		404 949	37 204	
Adjustment for first implementation of IPSAS	(note 3)				(378 456)	56 622	(321 834)
As at 1 January 2012 (restated per IPSAS)		**17 375**		**25 638**	**27 321**	**212 562**	**282 896**
Changes in net assets/equity for 2012							
Surplus (deficit) for the period					(77 063)	29 612	(47 451)
Gain/loss on revaluation of derivative financial instruments		(17 375)					(17 375)
Reserves, microcredit community support programme and Microfinance Department, during 2012				118			118
Actuarial (loss) on staff termination liabilities			(11 555)				(11 555)
Total net assets/equity			**(11 555)**	**25 756**	**(49 742)**	**242 174**	**206 633**

United Nations Relief and Works Agency for Palestine Refugees in the Near East

Statement IV
Cash flow for the year ended 31 December 2012
(Thousands of United States dollars)

	31 December 2012
Cash flows from operating activities	
Deficit for the year	(47 451)
Adjustment for non-cash items	
Add depreciation	22 933
Loss on disposal	1 422
Impairment of property, plant and equipment	679
Actuarial loss on employee benefit liabilities	(11 555)
Revaluation gain on derivative	(17 375)
Increase in allowance for doubtful debts	4 748
(Less) increase in inventories	(1 019)
(Less) increase in contributions receivable	(1 449)
(Less) increase in accounts receivable	(23 250)
Add decrease in loans receivable	1 830
Add decrease in other assets	186
(Add) increase in accounts payable and accruals	2 084
Add increase in leave encashment and employee benefits	54 494
Add increase in other liabilities	7 610
Add increase in advance contributions	2 916
Net cash from operating activities	**(3 198)**
Cash flows from investing activities	
Payments for property, plant and equipment	(47 973)
Payments for intangible assets	(6 724)
Decrease in investments	20 197
Net cash from investing activities	**(34 500)**
Cash flows from financing activities	
Add increase in capital reserve for Microfinance Department and microcredit community support programme	118
Net cash from financing activities	**118**
Net decrease in cash	(37 580)
Cash balance at the beginning of the year	270 013
Cash balance at the end of the year	**232 433**

United Nations Relief and Works Agency for Palestine Refugees in the Near East

Statement V

Comparison of budget and actual amounts for the year ended 31 December 2012

(Thousands of United States dollars)

		Budget amounts[a]			
	Note	*Original*	*Final*	*Actual on comparable basis*	*Variances: final budget and actual*
Revenue					
Cash contributions[b]		855 733	921 121	716 623	204 498
In-kind contributions		1 900	9 015	2 917	6 098
Interest on bank deposits		3 000	1 754	1 095	659
Other revenue					
Foreign currency exchange gain				2 192	(2 192)
Programme support cost recovery		20 000	21 778	21 778	
Financial derivative gain/loss				11 232	(11 232)
Miscellaneous revenue				5 240	(5 240)
Total revenue	**33**	**880 633**	**953 668**	**761 077**	**192 591**
Expenses					
Wages, salaries and employee benefits		506 281	541 302	552 626	(11 324)
Supplies and consumables		75 564	64 445	41 655	22 790
Occupancy, utilities and premises costs		16 664	13 586	11 006	2 580
Contracted services		295 433	198 783	87 127	111 656
Programme support cost		35 570	25 384		25 384
Cash subsidies		83 319	76 706	57 405	19 301
Depreciation		1 010	21 512	22 667	(1 155)
Provision and write-offs				5 598	(5 598)
Loss on disposal				1 422	(1 422)
Impairment of property, plant and equipment				679	(679)
Total expenses	**33**	**1 013 841**	**941 718**	**780 185**	**161 533**
Surplus/(deficit) for the year	**33**	**(133 208)**	**11 950**	**(19 108)**	**31 058**
Capital expenditure		–	103 163	48 176	54 996

[a] Includes general funds and projects (restricted funds, Microfinance Department and emergency appeals are not included).

[b] Includes General Fund, United Nations assessed contributions and projects (projects revenue is equivalent to the projects allocation in year 2012).

Notes to the financial statements

Note 1
Mission statement

The mission of the United Nations Relief and Works Agency for Palestine Refugees in the Near East (UNRWA) is to "help Palestine refugees achieve their full potential in human development under the difficult circumstances in which they live". The Agency fulfils this mission by providing a variety of essential services within the framework of international standards, to Palestine refugees in the Gaza Strip, the West Bank, Jordan, Lebanon and the Syrian Arab Republic. Among United Nations agencies, UNRWA is unique in terms of delivering services directly to refugees, and is similar in nature to a public service organization.

Note 2
Summary of significant accounting policies

(a) Basis of presentation

2.1 The financial statements have been prepared on the accrual basis of accounting, in accordance with the requirements of the International Public Sector Accounting Standards (IPSAS). Where IPSAS are silent concerning any specific matter, the appropriate International Financial Reporting Standard or International Accounting Standard is applied.

2.2 This is the first set of financial statements prepared in compliance with IPSAS. The adoption of IPSAS has required changes to be made to the accounting policies followed by the Agency. The adoption of the new accounting policies has resulted in changes to the assets and liabilities recognized in the statement of financial position. Accordingly, the previous audited statement of financial position, dated 31 December 2011, has been restated, and the resulting changes are reported in the statement of changes in net assets/equity and note 3, "Implementation of the International Public Sector Accounting Standards". The revised 31 December 2011 statement of financial position is described in these financial statements as the 1 January 2012 opening balance (restated). As permitted in respect of financial statements to which accrual accounting is first adopted in accordance with IPSAS, comparative information for the previous year has not been provided.

2.3 UNRWA has not applied the following new IPSAS, which have been issued but are not yet effective: Standard 28, "Financial instruments: presentation"; Standard 29, "Financial instruments: recognition and measurement"; and Standard 30, "Financial instruments: disclosures". The Standards on financial instruments will replace Standard 15, "Financial instruments: disclosure and presentation"; they establish principles for recognizing and measuring financial assets and financial liabilities, principles for presenting financial instruments as liabilities or net assets/equity, principles for offsetting financial assets and financial liabilities, and requirements for disclosure. The application of these Standards is required for reporting periods beginning on or after 1 January 2013. The impact of their initial application on the financial statements is expected to be minimal, owing to the limited use of financial instruments by UNRWA.

(b) Accounting convention

2.4 The financial statements have been prepared using the historical cost convention, except for certain financial instruments that are carried at fair value.

(c) Functional currency and translation of foreign currencies

Functional and presentation currency

2.5 The financial statements are presented in United States dollars, and all values are rounded to the nearest thousand. The functional currency of the Agency (including all fund groups) is the United States dollar, with the exception of the Microfinance Department, which uses the Syrian pound as the functional currency in the Syrian Arab Republic and the Jordanian dinar as the functional currency in the West Bank and Jordan.

Transactions and balances

2.6 Foreign currency transactions are translated into United States dollars using the United Nations operational rates of exchange, which approximate the exchange rates prevailing at the dates of the transactions. The United Nations operational rates of exchange are set once a month, and they are revised mid-month if there are significant exchange rate fluctuations relating to individual currencies.

2.7 Monetary assets and liabilities denominated in foreign currencies are translated into United States dollars at the year-end closing rate of the United Nations operational rates of exchange.

2.8 Both realized and unrealized foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation, at year-end exchange rates, of monetary assets and liabilities denominated in foreign currencies are recognized in the statement of financial performance.

Management of currency risks

2.9 The primary principle of the currency risk management policy of UNRWA is the preservation of the value of its financial resources in United States dollar terms. The Agency's currency risk can be identified mainly as a potential loss in the value of non-received non-United States dollar contributions and non-United States dollar cash assets as a result of a strengthening United States dollar. The risk arises from the date on which the contributions are pledged. In order to protect its assets and cash flow against adverse currency movements, UNRWA adopts a conservative risk management approach (hedging, for example) to minimize its exposure to exchange rate fluctuations. In order to hedge the currency risk, UNRWA entered into several forward contracts during the prior year that were settled in 2012. No such contracts were entered into in 2012 (refer to note 10).

2.10 These hedges are consistent with the Agency's risk management objective and strategy, as they remove the risk of an appreciation of the United States dollar and provide a fixed known income amount. The gain or loss from hedging will be offset by the foreign exchange gain or loss from donor contributions.

2.11 UNRWA provides protection against local currencies (currency adjustment factor) to its area staff for their salaries. The Agency's currency risk management policies allow hedging against local currencies to reduce the exposure due to fluctuations in exchange rates between the United States dollar and local currencies. At the end of the year, there were no outstanding hedging investments.

(d) Materiality and use of judgement and estimates

2.12 Materiality is central to the Agency's financial statements. The Agency's accounting materiality framework provides a systematic method for identifying, analysing, evaluating, endorsing and periodically reviewing materiality decisions crossing a number of accounting areas.

2.13 The financial statements necessarily include amounts based on judgements, estimates and assumptions by management. Changes in estimates are reflected in the period during which they become known.

(e) Significant accounting policies

Cash and cash equivalents

2.14 Cash and cash equivalents include cash on hand, cash at banks and other short-term highly liquid investments with original maturities of three months or less.

Contributions and contributions receivable

2.15 Contributions are recognized when confirmed in writing by donors or upon the submission and approval of the required report for subsequent payments in the case of multi-year contracts. When projects are coming to an end, and in the event that some contributions will not be fully expended on the project for which they were given, then at that point in time, and in accordance with the donor agreement, the amounts that will not be expended will be recognized as amounts to be refunded to donors and included in the statement of financial position and, as other income (expense), in the statement of financial performance. Contributions received from donors in advance are recorded as other liabilities in the statement of financial position until the criteria for recording revenue are met.

2.16 Contributions and contributions receivable are presented net of allowances for estimated reductions in contribution revenue and doubtful accounts.

2.17 In-kind contributions of services that directly support approved operations and activities, and that have budgetary impact and can be reliably measured, are recognized and valued at fair value. These contributions include the use of premises, vehicles and personnel.

2.18 Donated inventory or property, plant and equipment are valued at fair value and recognized as assets and revenue.

Accounts receivable

2.19 Receivables are recognized at their nominal value.

2.20 Allowances for doubtful accounts are recognized when there is objective evidence that a receivable is impaired. In particular, an allowance is recognized on the basis of historical collection experience. Impairment losses are recognized in the statement of financial performance.

2.21 Loans receivable and allowance for loan losses

2.21.1 *Loans receivable*

Loans receivable represent loans from borrowers under the Agency's microfinance programme and microcredit community support programme, which offer a number of targeted credit products through a revolving loan fund that serves its operations in all fields. Loans receivable are recognized at their outstanding principal balance.

2.21.2 *Provision for impairment of loans*

Each quarter, the Agency assesses whether a loan asset or group of loan assets is impaired. A group of loan assets is impaired and impairment losses are incurred only if there is objective evidence that there has been impairment as a result of one or more events ("loss events") occurring after the initial recognition of the asset and that the loss event or events have had an impact on the estimated future cash flows of the loan asset or group of loan assets that can be reliably estimated.

If, during the subsequent period, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is increased or reduced by adjusting the allowance account.

2.21.3 *Related-party ("insider") loans*

The Agency provides credit facilities to staff, but not to the Executive Director of the Microfinance Department or to members of the Advisory Board. The loan conditions and interest rates for staff-clients are identical to those for other customers. Such loans are provided for consumption and housing.

2.21.4 *Accrued interest on loans*

Interest income on loans financed is accounted for on the accrual basis.

2.21.5 *Recoveries*

Any recoveries of previously written-off loans are reflected in the statement of financial performance for the period during which they are received.

Financial instruments

2.22 Financial instruments are recognized when UNRWA becomes a party to the contractual provisions of the instrument until such time as the rights to receive cash flows from those assets have expired or have been transferred and UNRWA has transferred substantially all the risks and rewards of ownership.

2.23 Loans, receivables and payables are non-derivative financial instruments with fixed or determinable payments that are not quoted in active markets. These financial instruments comprise contributions receivable in cash, loans receivable as part of the credit facilities of the Microfinance Department, other receivables, cash in bank accounts and accounts payable. All non-derivative financial instruments are recognized in the statement of financial position at their fair values. The nominal value of receivables and payables approximates the fair value of the transaction.

2.24 UNRWA uses derivative financial instruments to hedge exchange risk. Foreign exchange forward contracts are revalued and the revaluation gain or loss is reported in the statement of financial performance if the contracts belong to the current year. For contracts related to subsequent years, the revaluation gain or loss is reported in the statement of financial position. For revaluation at year-end, the market rate for the forward contract is obtained from the banks and these are compared against the United Nations operational rate of exchange to ascertain the gain or loss.

Financial risk management

2.25 The activities carried out by UNRWA expose it to a variety of financial risks, primarily the effects of changes in foreign currency exchange rates. As a result, the Agency's financial risk management policies are focused on the unpredictability of foreign exchange rates and are aimed at minimizing, where feasible, potential adverse effects on the financial performance of UNRWA. Financial risk management is carried out by a central treasury function using UNRWA technical guidelines covering areas of financial risk such as foreign exchange, the use of derivative financial instruments and the investment of excess liquidity.

Advances and prepayments

2.26 Advances and prepayments are recognized at their nominal value.

Inventories

2.27 Inventories are stated at the lower of cost or current replacement cost. The cost of inventories includes purchase cost, or fair value if donated in kind, and all other costs incurred in bringing the inventory into custody.

2.28 Current replacement cost, which is used so that inventories can be distributed to beneficiaries at no or nominal charge, is the cost that the Agency would incur to acquire the asset on the reporting date.

2.29 Cost is determined using a weighted average cost formula.

2.30 A charge for impairment is recorded in the statement of financial performance for the year in which the inventory is determined to be impaired.

Property, plant and equipment

2.31 Property, plant and equipment items are stated at historical cost, less accumulated depreciation and any recognized impairment loss. For donated assets, fair value as at the date of acquisition is utilized as a proxy for historical cost. For property acquired before 1 January 2010, items were recognized at fair value as at that date and depreciated using the straight-line method over their estimated remaining useful lives.

2.32 Property, plant and equipment are capitalized in the financial statements if their cost exceeds a nominal value.

2.33 Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits or service potential associated with the item will flow to the Agency and the cost of the item can be measured reliably. All repairs and maintenance are charged to the statement of financial performance for the financial period during which they are incurred.

2.34 Depreciation is charged so as to allocate the cost of assets over their estimated useful lives using the straight-line method. The depreciation rates are as follows and are subject to annual review (property acquired before 2010 is not subject to the rates below):

(Percentage)

Asset type	*Depreciation rate*
Buildings and land improvements	
Buildings and land improvements	4
Prefabricated buildings	10
Short-life land improvements	14
Leasehold improvement	20
Vehicles	
Heavy trucks	5
Sedans, light buses and light trucks/buses	10
Other vehicles	14
Equipment	
Long-life information and communications technology (ICT) equipment, medical equipment and technical vocational training equipment	14
General machinery and equipment, office equipment, medium-life ICT equipment and teaching and school equipment	20
Short-life ICT equipment, computers and printers	33
Microfinance Department office equipment	10
Furniture and fixtures	
Fixtures	14
Furniture	10-20

Capital work in progress

2.35 All capital expenses incurred on construction are accumulated in a separate account within property, plant and equipment. On the completion of construction, the accumulated cost is transferred to a fixed asset account and depreciated on the basis of the aforementioned rates as at the date on which the completed asset is placed in service.

Intangible assets

2.36 Intangible assets are carried at historical cost, less accumulated amortization and any recognized impairment loss. For donated intangible assets, fair value as at the date of acquisition is used as a proxy for historical cost. Intangible assets are capitalized in the financial statements if their cost exceeds a nominal value.

2.37 Amortization is provided on a straight-line basis on all intangible assets of finite life, at rates that will allocate the cost or value of the assets to their estimated residual values. The estimated useful lives of major classes of intangible assets are as follows and are subject to annual review:

Asset class	*Useful life (years)*
Software acquired separately	3-6
Software internally developed	3-6
Licences and rights	2-6
Copyrights	3-10

2.38 Intangible asset recognition requires the meeting of strict criteria with respect to being identifiable, being under the Agency's control and contributing future economic benefits or service potential that can be reliably measured. Remaining useful life is also a consideration. Expenditure on research activities, undertaken with the prospect of gaining new scientific or technical knowledge and understanding, is expensed as incurred.

Software acquisition and development

2.39 Acquired computer software licences are capitalized on the basis of costs incurred to acquire the specific software and bring it into use. Costs directly associated with the development of software for use by the Agency are capitalized as an intangible asset. Development activities include a plan or design for the production of new or substantially improved products and processes. Development expenditure is capitalized only if the development costs can be measured reliably, the product or process is technically and commercially feasible, future economic benefits are probable, and UNRWA intends to and has sufficient resources to complete development and to use the asset. The expenditure capitalized includes the costs of materials and direct labour, overhead costs that are directly attributable to preparing the asset for its intended use. Other development expenditure is recognized in the statement of financial performance as incurred: capitalized development expenditure is measured at cost, less accumulated amortization and accumulated impairment losses.

Impairment

2.40 Assets that are subject to depreciation or amortization are reviewed annually for impairment to ensure that the carrying amount is still considered to be recoverable. Impairment occurs through complete loss, major damage or obsolescence. In the case of a complete loss, full impairment is recorded. This impairment loss can be reversed in subsequent periods, subject to a maximum of the impairment loss recognized.

Operating leases

2.41 Leases where the lessor retains a significant portion of the risks and rewards inherent to ownership are classified as operating leases. Payments due under operating leases are charged to the statement of financial performance as an expense.

Payables and accruals

2.42 Payables and accruals represent present obligations of the Agency arising from past events.

Employee benefits

2.43 UNRWA recognizes the following categories of employee benefits:

- Short-term employee benefits that fall due wholly within 12 months after the end of the accounting period during which employees render the related service;
- Post-employment benefits;
- Other long-term employee benefits;
- Termination benefits.

2.44 UNRWA is a member organization participating in the United Nations Joint Staff Pension Fund, which was established by the General Assembly to provide retirement, death, disability and related benefits to employees. The Pension Fund is a funded, multi-employer defined benefit plan. As specified in article 3 (b) of the Regulations of the Fund, membership in the Fund shall be open to the specialized agencies and to any other international, intergovernmental organization which participates in the common system of salaries, allowances and other conditions of service of the United Nations and the specialized agencies. All international staff members participate in the Fund.

2.45 The plan exposes participating organizations to actuarial risks associated with the current and former employees of other organizations participating in the United Nations Joint Staff Pension Fund, with the result that there is no consistent and reliable basis for allocating the obligation, plan assets and costs to individual organizations participating in the plan. Neither the Fund nor UNRWA, nor any other organization participating in the Fund, is in a position to identify its respective proportionate share of the defined benefit obligation, plan assets and costs associated with the plan with sufficient reliability for accounting purposes. Hence, UNRWA has treated this plan as if it were a defined contribution plan in accordance with the requirements set out in International Public Sector Accounting Standard 25. The Agency's contributions to the plan during the financial period are recognized as expenses in the statement of financial performance.

2.46 All area staff members participate in the Area Staff Provident Fund, which is accounted for as a defined contribution retirement plan in accordance with Standard 25.

Provisions and contingent liabilities

2.47 Provisions are made for future liabilities and charges where UNRWA has a present legal or constructive obligation as a result of past events, it is probable that UNRWA will be required to settle the obligation, and the amount can be reasonably estimated.

2.48 Other material commitments, which do not meet the recognition criteria for liabilities, are disclosed in the notes to the financial statements as contingent liabilities when their existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of UNRWA.

Interest revenue

2.49 Interest revenue is recognized over the period during which it is earned. The amount of interest on bank deposits is $1,155,000.

Programme support cost recovery

2.50 UNRWA is entitled to a specific percentage of the expenditures incurred on certain projects according to agreements with donors. Programme support cost recoveries are recognized as income and represent recoveries of overhead costs incurred by the Agency to implement the related projects. The amount of programme support cost recovery is $167,000.

Fund accounting and segment reporting

2.51 A fund is a self-balancing accounting entity established to account for the transactions of a specified purpose or objective. Funds are segregated for the purpose of carrying out specific activities or attaining certain objectives in accordance with special regulations, restrictions or limitations. The financial statements are prepared on a fund accounting basis, showing at the end of the period the consolidated position of all UNRWA funds. Fund balances represent the accumulated residual of revenue and expenses.

2.52 A segment is a distinguishable activity or group of activities for which financial information is reported separately in order to evaluate an entity's past performance in achieving its objectives and for making decisions about the future allocation of resources. UNRWA classifies all projects, operations and fund activities into four segments:

- Unearmarked activities;
- Earmarked activities, which include:
  - Restricted activities: a series of recurring activities aimed at bringing about clearly specified objectives within a defined time period and a defined budget. This applies to activities related to both cash and in-kind contributions;
  - Emergency appeals: activities under an external funding request to respond to a rapid crisis or a protracted humanitarian crisis with emergency operations;
  - Projects: used to meet capital expenditure or development needs to improve or supplement existing programmes and systems;
  - Microfinance: used to provide credit for enterprise activities, household consumption and housing needs that will improve the quality of life of householders and small-business owners and will help sustain jobs, reduce poverty, empower women and provide income-generating opportunities for Palestine refugees.

Budget comparison

2.53 The Agency's original budget is prepared on a commitment basis, and the final budget is prepared on an accrual basis. The financial statements are prepared on an accrual basis and compared against the final budget, which is prepared on a comparable basis.

2.54 The budget for the biennium 2012-2013 was submitted to the General Assembly. After consideration by the Assembly, the allocation and the appropriations were carried out by exercising the delegated authority.

Note 3
Implementation of the International Public Sector Accounting Standards

3.1 This is the first set of UNRWA financial statements that have been prepared on a full accrual basis and that comply with the requirements set out in IPSAS. Previous UNRWA financial statements were prepared to conform to the United Nations system accounting standards, and were presented on a modified cash basis; however, some IPSAS standards were implemented on a transitional basis. Under the United Nations system accounting standards, the financial statements were prepared on a biennial basis. The financial statements are prepared on an annual basis under IPSAS. The table below summarizes the adjustments made to the audited 2011 statement of assets, liabilities, reserves and fund balances to incorporate the changes in accounting policy in order to produce an IPSAS-compliant opening statement of financial position as at 1 January 2012.

Effect of initial implementation of the International Public Sector Accounting Standards

(Thousands of United States dollars)

	United Nations system accounting standards 31 December 2011	*Effect of transition to IPSAS, including adjustment*	*IPSAS 1 January 2012*
Assets			
Current assets			
Cash and cash equivalents	270 013	–	270 013
Short-term loans receivable	23 472	–	23 472
Contributions receivable	10 511	7 344	17 855
Accounts receivable	79 751	(45 347)	34 404
Other current assets	4 517	–	4 517
Inventories	28 613	–	28 613
Derivative financial instruments	–	20 197	20 197
Total current assets	**416 877**	**(17 806)**	**399 071**
Non-current assets			
Long-term loan receivable	1 603	–	1 603
Property, plant and equipment, net of depreciation	418 803	(3 970)	414 833

	United Nations system accounting standards 31 December 2011	Effect of transition to IPSAS, including adjustment	IPSAS 1 January 2012
Intangible assets	150	–	150
Total non-current assets	**420 556**	**(3 970)**	**416 586**
Total assets	**837 433**	**(21 776)**	**815 657**
Liabilities			
Current liabilities			
Payables and accruals	58 520	1 412	59 932
Employee benefits	29 764	30 828	60 592
Other current liabilities	4 140	(993)	3 147
Reserve for unliquidated obligations	113 323	(113 323)	–
Advance contributions	17 082	–	17 082
Total current liabilities	**222 829**	**(82 076)**	**140 753**
Non-current liabilities			
Employee benefits	–	382 133	382 133
Other non-current liabilities	9 875	–	9 875
Total non-current liabilities	**9 875**	**382 133**	**392 008**
Total liabilities	**232 704**	**300 057**	**532 761**
Net assets	**604 729**	**(321 833)**	**282 896**
Equity			
Other reserve	459 528	(442 153)	17 375
Capital reserve: microcredit community support programme and Microfinance Department	25 638	–	25 638
Accumulated surplus/(deficit)	119 563	120 320	239 883
Total equity	**604 729**	**(321 833)**	**282 896**
Total liabilities and equity	**837 433**	**(21 776)**	**815 657**

3.2 The adjustments made to generate the 1 January 2012 statement of financial position resulted in a $321,833,000 reduction in total equity. The principal adjustments can be analysed as indicated below.

Contributions receivable

3.3 Under the United Nations system accounting standards, contributions receivable were recognized only for the unearmarked funds within the General Fund. Under IPSAS, UNRWA now recognizes contributions receivable for project funds, emergency appeals and earmarked funds within the General Fund, resulting in an increase in equity of $7,344,000. An allowance is netted from contributions receivable to reflect the amount considered unlikely to be received. The following receivables have been included under the IPSAS accounting policy:

(Thousands of United States dollars)

	1 January 2012
Contributions receivable for project funds	4 552
Contributions receivable for emergency appeals	7 515
Contributions receivable for restricted funds	145
Contributions receivable for unearmarked funds	721
Provision for uncollectible contributions	(5 589)
Net effect on equity	**7 344**

Accounts receivable

3.4 The change in policy for the calculation of allowances for doubtful debts in accounts receivable and the reclassification of derivative financial instruments in accordance with IPSAS has resulted in a reduction in equity of $25,150,000 as follows:

(Thousands of United States dollars)

	1 January 2012
Increase in provision for value-added tax due from the Palestinian Authority	(24 615)
Provision for refundable utility deposits	(127)
Provision for claims against Governments	(131)
Provision for personal accounts	(207)
Provision for other receivables	(70)
Net effect on equity	**(25 150)**
Reclassification of derivative financial instruments	(20 197)
Total	**(45 347)**

Derivative financial instruments

3.5 Derivative financial instruments in the amount of $20,197,000 were included in accounts receivable balances under the United Nations system accounting standards. Under IPSAS, they have been reclassified as deferred revenue within liabilities. There is no effect on equity as a result of this change.

Property, plant and equipment

3.6 Work in progress for capital projects was included in the 2011 closing balance under the United Nations system accounting standards. The capital work in progress, totalling $17,530,000, was related to camp improvements and assets that UNRWA provides to beneficiaries but does not own. This was therefore removed from the IPSAS opening balance. Additionally, property, plant and equipment totalling $8,744,000 and work in progress on capital projects totalling $4,816,000 were omitted from the 2011 closing balance under the United Nations system accounting standards. These have now been properly included in the opening balance for 2012 under IPSAS, resulting in a net decrease in equity of $3,970,000.

Accounts payable

3.7 The recording of accruals for goods and services delivered but remaining unpaid as at the end of 2011 resulted in an increase in liabilities of $1,412,000.

Employee benefit liabilities

3.8 Accumulated annual leave for area staff was recognized under the United Nations system accounting standards. Under IPSAS, end-of-service employee benefits have been recognized for area staff and for international staff not funded through the United Nations regular budget. End-of-service benefits for area staff cover separation costs on normal retirement, early voluntary retirement, termination costs, disability benefits and death-in-service benefits. These additional liabilities have resulted in a reduction in equity of $412,961,000, as follows:

(Thousands of United States dollars)

	1 January 2012
Recognition of end-of-service benefits for area staff	(410 668)
Recognition of end-of-service benefits for international staff	
Repatriation grant	(597)
Shipment costs	(598)
Travel costs	(178)
Outstanding annual leave	(439)
After-service health insurance	(481)
Net effect on equity	**(412 961)**

3.9 The increased liability comprised $30,828,000 in current liabilities and $382,133,000 in non-current liabilities.

Other liabilities

3.10 Other liabilities were reduced by $993,000 to remove obligations that do not meet the criteria for recognition as a liability under IPSAS.

Unliquidated obligations

3.11 Liabilities relating to unliquidated obligations are no longer recognized in the financial statements under IPSAS, as they do not correspond to the recognition of expenses in accordance with accrual accounting. This adjustment has resulted in a reduction in liabilities of $113,323,000, with a corresponding increase in equity.

Note 4
Cash and cash equivalents

4.1 Cash is held principally in United States dollar bank accounts. The composition of cash is as follows:

(Thousands of United States dollars)

	31 December 2012	1 January 2012 (restated)
Cash in hand	1 747	2 552
Cash at banks	230 686	180 332
Short-term investments with original maturity less than 3 months	–	87 129
Total	**232 433**	**270 013**

4.2 The Agency held funds for other United Nations entities in the amount of $1,869,000 at 31 December 2012 and $2,226,000 at 1 January 2012 (restated under IPSAS).

4.3 The balances of cash and cash equivalents on hand as at 31 December 2012 were held in the currencies shown in the table below. Currency values have been converted at the United Nations official rates of exchange as at 1 January 2013.

	Balance as at 31 December 2012			*Balance as at 1 January 2012*		
Currency	*Currency amount (thousands)*	*United Nations official rate of exchange*	*United States dollar amount (thousands)*	*Amount*	*United Nations official rate of exchange*	*United States dollar amount (thousands)*
Australian dollar	0	0.965	0	(15)	0.991	(15)
Canadian dollar	231	0.993	233	235	1.024	230
Swiss franc	341	0.911	374	559	0.945	592
Danish krone	500	5.621	89	169	5.755	29
Egyptian pound	(8)	6.188	(1)	147	6.010	24
Euro	14 652	0.754	19 432	7 865	0.774	10 162
Pound sterling	1 876	0.619	3 030	925	0.648	1 427
Jordanian dinar	4 578	0.708	6 466	19 547	0.708	27 609
Yen	630 132	86.070	7 321	130	77.800	2
Lebanese pound	312 117	1 499	208	7 402 593	1 500	4 935
New Israeli sheqel	5 502	3.722	1 478	10 593	3.780	2 802
Norwegian krone	20 030	5.562	3 601	994	6.020	165
Swedish krona	301	6.488	46	999	6.919	144
Syrian pound	88 763	74.370	1 194	1 011 428	55.260	18 303
United States dollar	187 215	1.000	187 215	201 051	1.000	201 051
Cash at banks			230 686			267 460
Cash on hand			1 747			2 552
Total			**232 433**			**270 013**

Note 5
Loans receivable

5.1 Loans receivable include loans outstanding from funds disbursed from the Microfinance Department and the microcredit community support programme both through an initial donor contribution (first-time loans) and from revolving loan funds. The Microfinance Department operates as a separate department within UNRWA. The microcredit community support programme is a subprogramme of the Social Services Division of the Relief and Social Services Department of UNRWA.

5.2 The composition of loans receivable, net of allowance for bad debts by maturity, is as follows:

(Thousands of United States dollars)

	31 December 2012			*1 January 2012 (restated)*		
	Microfinance Department	*Microcredit community support programme*	*Total*	*Microfinance Department*	*Microcredit community support programme*	*Total*
Current	18 256	1 165	19 421	21 203	2 269	23 472
Non-current	1 871	806	2 677	1 603	–	1 603
Total	**20 127**	**1 971**	**22 098**	**22 806**	**2 269**	**25 075**

Provision for loans receivable

5.3 The change in the allowance for doubtful loans receivable is as follows:

(Thousands of United States dollars)

	Allowance for doubtful loans receivable		
	Microfinance Department	*Microcredit community support programme*	***Total***
Beginning balance as at 1 January 2012	(1 390)	(20)	**(1 410)**
Additions	(1 986)	–	**(1 986)**
Less: write-off	837	2	**839**
Ending balance	**(2 539)**	**(18)**	**(2 557)**

Allowance for loan losses

5.4 For the microcredit community support programme, the provision for doubtful loans is equal to 3 per cent of the outstanding amount of the loan portfolio excluding loans to UNRWA staff, for which no provision is made.

5.5 For the Microfinance Department, the provision for doubtful loans is based on an “aged portfolio at-risk report” (see below), which is applied to the total amount outstanding of each loan. On the basis of empirical experience, historical record and market knowledge, it was determined that the following general provision is required for delinquent and defaulting Microfinance Department loans:

Loan status	*Allowance*
Current	1% general provision
1-30 days overdue	5% general provision
31-60 days overdue	10% general provision
61-90 days overdue	25% general provision
91-120 days overdue	50% general provision
121-180 days overdue	75% general provision
181-360 days overdue	100% general provision

5.6 Effective September 2012, a special impairment on outstanding Microfinance Department loans was adopted in the Syrian Arab Republic to mitigate the risk posed by the situation of armed conflict. The rates of reserve calculation are set out below for the special impairment at year-end 2012:

Loan status	*Allowance*
1-30 days overdue	95% special impairment
31-60 days overdue	90% special impairment
61-90 days overdue	75% special impairment
91-120 days overdue	50% special impairment
121-180 days overdue	25% special impairment
181-360 days overdue	0% special impairment

5.7 Based upon the above percentages, if a loan is not serviced, an increasing reserve should be provided for. This provision will be shown in the statement of financial performance for the period. On a monthly basis, an adjustment is made to reflect the changes in the general provision. After a loan is in arrears for 360 days or more and has been fully provisioned in the general provision, a write-off will take place. Recovery of written-off loans will continue to be pursued through the collection and compliance section of the Department.

Note 6
Contributions receivable

6.1 Contributions receivable represent confirmed pledges outstanding from donors that are due within 12 months. The following is a breakdown of contributions receivable balances by donor category at the end of the year:

(Thousands of United States dollars)

	31 December 2012	*1 January 2012 (restated)*
Due from Governments	3 979	7 954
Due from intergovernmental organizations	20 483	15 155
Due from United Nations organizations	431	335
Provision against contributions receivable	(2 092)	(5 589)
Total contributions receivable	**22 801**	**17 855**

6.2 There are no non-current receivables due after 12 months from 31 December 2012.

6.3 Contributions receivable relate to donor contributions for each of the five identified segments. Donor contributions may include restrictions that require UNRWA to use the contribution for a specific project, activity or country within a specified time period.

6.4 Contributions receivable are shown net of allowances for estimated reductions in contribution revenue and doubtful accounts.

6.5 The change in the allowance for doubtful contributions receivable is as follows:

(Thousands of United States dollars)

Beginning balance as at 1 January 2012	5 589
Reduction in provision	(3 042)
Less: write-off	(455)
Ending balance	**2 092**

6.6 The allowance for doubtful contributions receivable is estimated at the following percentages of outstanding contributions receivable:

(Percentage)

Governments	Less than 2 years	0
	From 2 years to less than 3 years	50
	3 years or more	100

6.7 After six years, the doubtful debt and the write-off request, together with the supporting documents, should be submitted to the Director of Finance for approval after all collection efforts have been exhausted.

Note 7
Accounts receivable

7.1 Accounts receivable are due to be collected within 12 months and comprise the following:

(Thousands of United States dollars)

	Relevant note	*31 December 2012*	*1 January 2012 (restated)*
Value-added tax receivable	7.1.1	76 648	55 941
Other accounts receivable	7.1.2	9 592	6 360
Due from Area Staff Provident Fund		464	1 154
Less provisions	7.1.3	(36 149)	(29 051)
Accounts receivable net of provisions		**50 555**	**34 404**

Value-added tax receivable

7.1.1 Value-added tax receivable represents amounts receivable from Governments for value-added tax paid by the Agency that is subject to reimbursement.

Other accounts receivable

7.1.2 Other accounts receivable comprise the following:

(Thousands of United States dollars)

	31 December 2012	*1 January 2012 (restated)*
From Governments	134	134
Miscellaneous receivable	4 066	3 129
Personal accounts of staff members	5 253	2 965
Refundable utility deposits	139	132
Total	**9 592**	**6 360**

7.1.3 Provisions

(Thousands of United States dollars)

	Value-added tax	*Accounts receivable*	***Total***
Beginning balance as at 1 January 2012	(27 767)	(1 284)	**(29 051)**
Additions	(7 147)	(534)	**(7 681)**
Less: write-off		583	**583**
Ending balance	**(34 914)**	**(1 235)**	**(36 149)**

7.2 The provisions for value-added tax receivable and accounts receivable are estimated amounts based on the aged analysis of the outstanding amounts as at the reporting date. These provisions have been calculated on the basis of past experience and the likelihood of collecting the outstanding amounts over the specific periods, as shown in the table below.

(Percentage)

Value-added tax receivable	Less than 2 years	0
	From 2 years to less than 3 years	50
	3 years or more	100
Other receivable	1 year or more	100

7.3 After six years for value-added tax receivable and three years for other receivables, the doubtful debt and the write-off request, together with the supporting documents, may be submitted to the Director of Finance for approval after all collection efforts have been exhausted. In some instances, collection efforts continue after the time periods specified above have elapsed.

Note 8
Other assets

8.1 Included in other assets are prepaid expenses and advances to suppliers. Prepaid expenses and advances to suppliers totalled $4,331,000 at 31 December 2012 and $4,517,000 as at 1 January 2012 (restated under IPSAS). Included in these amounts are prepayments to staff in the amount of $381,000 as at 31 December 2012 and $730,000 as at 1 January 2012 (restated under IPSAS).

8.2 The composition of prepaid expenses and advances to suppliers as at 31 December 2012 is shown in the table below. The full amount of non-current assets represents advances to suppliers.

(Thousands of United States dollars)

	31 December 2012	*1 January 2012 (restated)*
Current	3 977	4 517
Non-current	354	–
Total	**4 331**	**4 517**

Note 9
Inventories

9.1 Inventories consist of the following:

(Thousands of United States dollars)

Type	*31 December 2012*	*1 January 2012 (restated)*
Warehouse	23 253	24 867
Pharmacy/clinic	3 256	3 603
In transit	2 927	–
Production unit	196	143
Total	**29 632**	**28 613**

9.2 Warehouse inventory comprises four main categories of items that are distributed to refugees or used to provide services to refugees: medical supplies, general supplies, food, and motor transport.

9.3 Pharmacy/clinic inventory represents medical supplies distributed from the warehouse and held in the respective pharmacies and clinics for the five fields.

9.4 Production unit inventory relates to the Agency's self-supporting production unit, which is the embroidery centre located in the Gaza Strip. This unit is governed by separate instructions for effective management control and performance assessment. Inventories of the production unit are reported at cost, under assets in the financial statements.

9.5 The components of the production unit inventory are as follows:

(Thousands of United States dollars)

	31 December 2012	*1 January 2012 (restated)*
Raw materials inventory — embroidery	73	64
Work in progress — embroidery	10	5
Finished goods — embroidery	113	74
Total	**196**	**143**

9.6 Impairment expense for inventory in the amount of $124,000 was recorded in 2012.

9.7 The Agency conducts stock counts of inventory on a quarterly basis. Owing to the armed conflict in the Syrian Arab Republic, the most recent comprehensive inventory stock count in this field was completed on 30 June 2012. The Agency tracks additions and reductions to inventory and utilized this information to arrive at the ending inventory value for the Syrian Arab Republic field as at 31 December 2012.

Note 10
Derivative financial instruments

Nature of financial instruments

10.1 Details of the significant accounting policies and methods adopted, including the criteria for recognition and de-recognition, the basis of measurement and the basis on which gains and losses are recognized in respect of each class of financial asset and financial liability, are set out in note 2.

10.2 These financial instruments of UNRWA comprise contributions receivable in cash, loans receivable as part of the credit facilities of the Microfinance Department, other receivables, cash in bank accounts and accounts payable.

Financial derivatives

10.3 All the opening outstanding financial derivative forward contracts were revalued as at 31 December 2011. The majority of the revaluations resulted in a revaluation gain, and a few resulted in a revaluation loss. The gain of $20,197,000 is disclosed as an asset in the statement of financial position, and the details are presented in the table below.

10.3.1 **Revaluation of 2012 contracts as at 31 December 2011**

Hedged items			*Hedged instruments*						
Donor contributions			*Foreign exchange forwards*				*Gain/(loss)*		
Currency	*Amount (thousands)*	*Expected receipt date*	*Currency hedged*	*Hedged amount (thousands)*	*Forward rate*	*Forward amount (thousands of United States dollars)*	*United Nations rate*	*Amount, United Nations rate (thousands)*	*Revaluation as at 31 December 2011 (thousands of United States dollars)*
Euro	50 000	March 2012	Euro	50 000	1.4096	70 480	1.2920	64 600	5 881
Euro	40 000	June 2012	Euro	40 000	1.5722	62 888	1.2920	51 680	11 209
Norwegian krone	150 000	March 2012	Norwegian krone	150 000	5.9916	25 035	6.0200	24 917	118
Danish krone	60 000	March 2012	Danish krone	60 000	5.1675	11 611	5.7550	10 426	1 185
Swedish krona	200 000	March 2012	Swedish krona	200 000	6.9122	28 934	6.9190	28 906	28
Swiss franc	8 000	March 2012	Swiss franc	8 000	0.7811	10 242	0.9450	8 466	1 776
Total classified as asset in statement of financial position									**20 197**

10.3.2 The revaluation of a few contracts resulted in a revaluation loss, and the loss of $2,822,000 is disclosed as a liability under accounts payable in the statement of financial position, as detailed below.

Revaluation of 2012 contracts resulting in a loss and classified as a liability in the statement of financial position as at 31 December 2011

Currency	*Amount (thousands)*	*Expected receipt date*	*Currency hedged*	*Hedged amount (thousands)*	*Forward rate*	*Forward amount (thousands of United States dollars)*	*United Nations rate*	*United Nations rate amount (thousands)*	*Revaluation as at December 2011 (thousands of United States dollars)*
Donor contributions hedged									
Pound sterling	10 000	June 2012	Pound sterling	10 000	1.2743	12 743	1.543	15 430	(2 689)
Currency	*Amount (equivalent in thousands of United States dollars)*	*Expected receipt date*	*Forward rate*	*Hedged amount (thousands)*	*Spot rate*	*New sheqel amount (thousands)*	*Fixing/ United Nations rate*	*Forward amount (thousands of United States dollars)*	*Gain/(loss) (thousands of United States dollars)*
Non-donor contributions hedged									
New sheqel	14 500	January 2012	3.7639	14 500	3.8221	55 420	3.78	14 458	(43)
New sheqel	14 500	February 2012	3.7652	14 500	3.8243	55 452	3.78	14 456	(44)
New sheqel	14 500	February 2012	3.7662	14 500	3.8259	55 476	3.78	14 454	(46)
Total classified as a liability in the statement of financial position									**(2 822)**

10.3.3 In 2012, all outstanding contracts from the previous year matured and UNRWA did not enter into new derivatives contracts. Hence, there are no outstanding contracts as at 31 December 2012, and consequently no corresponding revaluation gain or loss.

10.3.4 The forward contracts that matured in 2012 resulted in a realized gain of $11,232,000 during the year; the details are shown below. This gain is disclosed in the statement of financial performance.

Realized gains on forward contracts matured in 2012

Currency	*Amount (thousands)*	*Valuation date*	*Bank*	*Outright*	*Amount received (thousands of United States dollars)*	*Status*	*United Nations rate*	*Gain/(loss) (thousands of United States dollars)*
Euro	50 000	26 March 2012	BNP	1.4104	70 520	Settled	1.340	3 496
Norwegian krone	150 000	26 March 2012	HSBC	5.5925	26 822	Settled	5.587	(26)
Danish krone	60 000	26 March 2012	BNP	5.2866	11 349	Settled	5.549	537
Swedish krona	200 000	26 March 2012	HSBC	6.4488	31 014	Settled	6.595	688
Swiss franc	8 000	26 March 2012	BNP	0.9181	8 714	Settled	0.897	(205)
Euro	40 000	25 June 2012	BNP	1.4065	56 260	Settled	1.242	6 571
Pound sterling	10 000	25 June 2012	BNP	1.6134	16 134	Settled	1.558	558
Danish krone	50 000	26 April 2012	BNP	5.6498	8 850	Settled	5.600	(79)
Swiss franc	5 000	26 April 2012	BNP	0.9169	5 453	Settled	0.907	(60)
Swiss franc	5 000	29 May 2012	BNP	0.9082	5 505	Settled	0.907	(7)
Euro	(32 000)	25 June 2012	BNP	1.2513	(40 042)	Settled	1.242	(290)
Euro	32 000	25 July 2012	BNP	1.2513	40 043	Settled	1.244	240
Subtotal								**11 423**

Non-donor contributions hedged

Currency	*Amount (thousands of United States dollars)*	*Fixing date*	*Bank*	*Outright*	*Fixing rate*	*Status*	*United Nations rate*	*Gain/(loss) (thousands of United States dollars)*
New sheqel	14 500	10 January 2012	BNP	3.7639	3.8403	Settled	3.8403	(288)
New sheqel	14 500	10 February 2012	BNP	3.7652	3.7223	Settled	3.7300	167
New sheqel	14 500	12 March 2012	BNP	3.7662	3.7845	Settled	3.7200	(70)
Subtotal								**(191)**
Total realized gains on forward contracts								**11 232**

Credit risk

10.4 UNRWA has limited credit risk, because its donors are generally of a high credit standing. Contributions receivable comprise primarily amounts due from sovereign nations. Details of contributions receivable, including allowances for reductions in contribution revenue, are provided in note 6.

10.5 The greatest area of credit risk arises from loans provided by the Microfinance Department. The Department manages credit risk by:

- Establishing ceilings on amounts of direct credit for each product linked to the cash flow of each client;
- Providing a range of products to different sectors and segments to spread credit and reduce concentration;
- Formulating credit policies by product, covering collateral requirements and credit compliance with regulatory requirements in each jurisdiction;

- Establishing the authorization structure for the approval and renewal of credit facilities;
- Reviewing and assessing credit risk in excess of designated limits prior to facilities being committed to customers. Renewals of facilities are subject to the same process;
- Developing and maintaining a risk-grading system in order to categorize exposure according to when impairment provisions are required against specific credit exposures;
- Providing guidance and training to improve skills of staff in order to promote best practice in the management of credit risk.

10.6 In 2012, the credit risk in the Syrian Arab Republic and the Gaza Strip increased as a result of conflict. The Microfinance Department manages this risk by increasing provisions as the portfolio at risk increases as a percentage of the full portfolio.

10.7 UNRWA has its cash deposited with various banks, and is therefore exposed to the risk that a bank will default in its obligation towards the Agency. However, UNRWA holds all significant cash deposits in banks that have a “P-1” credit rating.

10.8 There is no perceived risk that other receivables may not be liquidated when they fall due.

Interest rate risk

10.9 UNRWA deposits its funds in short-term fixed interest accounts, and therefore has no significant interest rate risk exposure.

Foreign currency risk

10.10 UNRWA receives contributions from donors in currencies other than the primary currency of the expenditures, United States dollars. In 2012, 32 per cent of contributions were denominated in the United States dollar base currency and 68 per cent were denominated in other currencies. The Microfinance Department lends in different currencies in each of the Agency’s fields of operation, with the United States dollar used in the Gaza Strip, the Jordanian dinar used in Jordan and the West Bank, and the Syrian pound used in the Syrian Arab Republic.

10.11 Furthermore, some field office expenditures are incurred in non-United States dollar currencies. UNRWA is therefore exposed to foreign currency exchange risk arising from fluctuations of currency exchange rates. Foreign exchange forward contracts are used to hedge the non-United States dollar exchange exposure for donor contributions, as well as some field office costs.

10.12 In order to protect its assets and cash flow against adverse currency movements, UNRWA adopts a conservative risk management approach, hedging to minimize its exposure to exchange rate fluctuations. In order to hedge the currency risk, UNRWA enters into forward contracts to remove the risk of an appreciation of the United States dollar and to provide a known, fixed income amount.

10.13 During the year ended 31 December 2012, 10 contracts were settled. No new contracts were entered into in 2012. At 31 December 2012, UNRWA had no unrealized contracts. The realized gains are included in the currency exchange differences presented in the statement of financial performance.

10.14 At 31 December 2012, 81 per cent of cash held in banks was denominated in the United States dollar base currency, 4 per cent was denominated in local currencies used by the UNRWA field offices to support operating activities, and the remaining cash at banks was held in other currencies. A full breakdown of cash held at banks in currencies other than the United States dollar is provided in note 4.

Note 11
Property, plant and equipment

The table below presents a summary of property, plant and equipment as at 31 December 2012.

(Thousands of United States dollars)

Description	*Land*	*Buildings*	*Leasehold improvements*	*Furniture and fittings*	*Office and computer equipment*	*Motor vehicles*	*Construction in progress*	*Assets not placed in service*	*Total*
Cost									
As at 1 January 2012 (restated)	16 250	374 845	514	483	27 853	31 717	24 481	976	**477 119**
+ Additions in 2012		24 056	–	475	4 034	2 049	16 930	431	**47 975**
(-) Disposals in 2012		1 190	–	25	145	546	–		**1 906**
Impairment in 2012		(594)	–	–	–	(85)	–		**(679)**
Balance as at 31 December 2012 (A)	**16 250**	**397 117**	**514**	**933**	**31 742**	**33 135**	**41 411**	**1 407**	**522 509**
Depreciation and impairment									
Balance at 1 January 2012 (restated)	–	30 721	339	82	14 708	16 436	–	–	**62 286**
Depreciation in 2012	–	16 022	60	96	4 471	2 284	–	–	**22 933**
(-) Depreciation on disposals in 2012	–	157	–	–	66	259	–	–	**482**
Balance as at 31 December 2012 (B)	**–**	**46 586**	**399**	**178**	**19 113**	**18 461**	**–**	**–**	**84 737**
Net book value as at 31 December 2012 (A minus B)	**16 250**	**350 531**	**115**	**755**	**12 629**	**14 674**	**41 411**	**1 407**	**437 772**

Note 12
Intangible assets

12.1 Intangible assets are summarized as follows:

(Thousands of United States dollars)

Class	*Beginning balance*	*Additions*	*Disposals*	*End balance*
Software acquired separately	150	378	–	528
Software internally developed	–	6 346	–	6 346
Licences and rights	–	–	–	–
Copyrights	–	–	–	–
Total	**150**	**6 724**	–	**6 874**

12.2 According to International Public Sector Accounting Standard 31, an entity that has not previously recognized intangible assets and uses the accrual basis of accounting shall apply that Standard prospectively. The Agency has applied Standard 31 prospectively as from 1 January 2012 and, accordingly, has recognized intangible assets acquired on or after that date. Except for software acquired separately by the Microfinance Department, intangible assets acquired prior to that date have not been recognized, owing to the fact that prior to 2012 there were no tracking mechanisms in place to provide a reliable cost determination.

12.3 In 2012, the Agency undertook a significant software development initiative related to a new enterprise resource planning system. This is a multi-year project and represents the total amount of computer software internally developed as shown in the table above.

12.4 All intangible assets are currently under construction, and therefore no amortization of intangible assets was recorded in 2012.

Note 13
Accounts payable and accruals

13.1 Accounts payable consist of the following:

(Thousands of United States dollars)

	Relevant note	*31 December 2012*	*1 January 2012 (restated)*
Supplier accounts payable	13.1.1	15 355	18 119
Financial derivative liability account		–	2 822
Accrued salaries and wages		2 239	–
Accrued expenses	13.1.2	32 458	29 578
Other accounts payable	13.1.3	11 963	9 413
Accounts payable, non-current	13.1.4	11 188	9 875
Total		**73 203**	**69 807**

The composition of accounts payable is as follows:

(Thousands of United States dollars)

	31 December 2012	1 January 2012 (restated)
Current	62 015	59 932
Non-current	11 188	9 875
Total	**73 203**	**69 807**

Supplier accounts payable

13.1.1 Supplier accounts payable represent outstanding amounts payable to vendors for goods and services received.

Accrued expenses

13.1.2 Accrued expenses include the following:

(Thousands of United States dollars)

	31 December 2012	1 January 2012 (restated)
Accrued expenses for services and utilities	30 949	25 090
Area staff group medical insurance	869	2 925
Accrued salaries, wages and other expenses	444	600
Other salary related payable	–	670
Payable — reclassifications of accounts receivable balance staff	196	263
Total	**32 458**	**29 578**

Other accounts payable

13.1.3 Other accounts payable consist of the following:

(Thousands of United States dollars)

	31 December 2012	1 January 2012 (restated)
Deposits received	228	375
West Bank water supply, Palestinian Authority	69	–
Unpaid cheques	200	439
Funds held for other United Nations entities	1 869	2 226
Interest payable for projects	3 494	3 787
Miscellaneous accounts payable	2 606	2 586
Accounts payable — goods in transit	463	–
Staff liabilities payable	3 034	–
Total	**11 963**	**9 413**

Accounts payable, non-current

13.1.4 Accounts payable, non-current consist of the following:

(Thousands of United States dollars)

	31 December 2012	*1 January 2012 (restated)*
OPEC Fund for International Development PalFund Trust Fund — Microfinance Department	9 875	9 875
Vendor balances, non-current	1 313	–
Total	**11 188**	**9 875**

Note 14
Employee pension fund

14A
UNRWA Area Staff Provident Fund

14A.1 The UNRWA Area Staff Provident Fund, established under article XIII of the Agency's Financial Regulations, is a retirement benefit plan that applies to all area staff members and vests after six months of service. UNRWA has treated this plan as if it were a defined contribution plan in accordance with the requirements of International Public Sector Accounting Standard 25. The Agency's contributions to the plan during the financial period are recognized as expenses in the statement of financial performance.

The balances outstanding with the Provident Fund as at 31 December 2012 are shown below.

(Thousands of United States dollars)

	31 December 2012	*1 January 2012 (restated)*
Opening balance	(1 154)	73
Employee contributions	40 552	71 989
Agency contributions	67 930	111 826
Withdrawals	(83 029)	(148 593)
Area Staff Provident Fund employee loans	(24 864)	(36 606)
Area Staff Provident Fund loan commission	101	157
Total	**(464)**	**(1 154)**

14B
United Nations Joint Staff Pension Fund: international staff

14B.1 The Regulations of the United Nations Joint Staff Pension Fund state that the Pension Board shall have an actuarial valuation made of the Fund at least once every three years by the consulting actuary. The practice of the Pension Board has been to carry out an actuarial valuation every two years using the open group aggregate method. The primary purpose of the actuarial valuation is to determine whether the current and estimated future assets of the Pension Fund will be sufficient to meet its liabilities.

14B.2 The Agency's financial obligation to the Pension Fund consists of its mandated contribution, at the rate established by the General Assembly (currently 7.9 per cent for participants and 15.8 per cent for member organizations), together with any share of any actuarial deficiency payments under article 26 of the Regulations of the Fund. Such deficiency payments are payable only if and when the provision of article 26 is invoked by the Pension Board, following a determination that there is a requirement for deficiency payments based on an assessment of the actuarial sufficiency of the Pension Fund as at the valuation date. Each member organization shall contribute to this deficiency an amount proportionate to the total contributions that each paid during the three years preceding the valuation date.

14B.3 The latest actuarial valuation was performed as at 31 December 2011. The valuation revealed an actuarial deficit of 1.87 per cent (compared with 0.38 per cent in the 2009 valuation) of pensionable remuneration, implying that the theoretical contribution rate required to achieve balance as at 31 December 2011 was 25.57 per cent of pensionable remuneration, compared with the actual contribution rate of 23.7 per cent. The actuarial deficit was attributable primarily to the lower-than-expected investment experience in recent years.

14B.4 At 31 December 2011, the funded ratio of actuarial assets to actuarial liabilities, assuming no future pension adjustments, was 130 per cent (compared with 140 per cent in the 2009 valuation). The funded ratio was 86 per cent (compared with 91 per cent in the 2009 valuation) when the current system of pension adjustments was taken into account.

14B.5 After assessing the actuarial sufficiency of the Fund, the consulting actuary concluded that there was no requirement, as at 31 December 2011, for deficiency payments under article 26 of the Regulations of the Fund, as the actuarial value of assets exceeded the actuarial value of all accrued liabilities under the Fund. The market value of assets also exceeded the actuarial value of all accrued liabilities as at the valuation date. At the time of reporting, the General Assembly had not invoked the provision of article 26. The pensionable remuneration will be reviewed at the time of the next actuarial valuation, as at 31 December 2013.

14B.6 In August 2012, the Pension Board noted, in its report on its fifty-ninth session to the General Assembly (A/67/9), that an increase in the normal age of retirement for new participants in the Fund to 65 was expected to significantly reduce the deficit and would potentially cover half of the current deficit of 1.87 per cent. In December 2012, the Assembly authorized the Pension Board to increase the normal retirement age to 65 for new participants in the Fund, with effect not later than 1 January 2014, unless the Assembly has not decided on a corresponding increase in the mandatory age of separation.

14B.7 For 2012, contributions paid to the Pension Fund amounted to $7,310,000, compared with $7,018,000 for 2011. The contributions due in 2013 are expected to amount to $7,606,000.

14B.8 The Board of Auditors carries out an annual audit of the Pension Fund and reports to the Pension Board on the audit every year. The Fund publishes quarterly reports on its investments; these can be viewed by visiting the Fund's website (www.unjspf.org).

Note 15
Staff end-of-service and termination benefits

15.1 UNRWA recognizes the following categories of employee benefits:

- Short-term employee benefits due to be settled within 12 months after the end of the accounting period during which employees render the related service;
- Post-employment benefits;
- Other long-term employee benefits;
- Termination benefits.

(Thousands of United States dollars)

	31 December 2012	*1 January 2012 (restated)*
Current	63 648	60 592
Non-current	433 571	382 133
Total	**497 219**	**442 725**

(Thousands of United States dollars)

	31 December 2012	*1 January 2012 (restated)*
Annual leave encashment for area staff	31 975	27 868
End-of-service liability for area staff	463 018	412 564
Short-term employee benefits for international staff not funded through the United Nations regular budget	1 434	1 812
Long-term employee benefits for international staff not funded through the United Nations regular budget	792	481
Total	**497 219**	**442 725**

Short-term employee benefits for area staff

15.2 Short-term employee benefits consist of the annual leave of area staff. The amount of liability is calculated on the basis of the accumulated leave balances in the human resources module as at 31 December 2012. The total employee annual leave liability as at 31 December 2012 amounted to $31,975,000.

End-of-service liabilities for area staff

15.3 Area staff end-of-service and termination benefit liabilities are determined by professional actuaries or calculated by UNRWA on the basis of personnel data and past payment experience. At 31 December 2012, total employee benefits liabilities amounted to $463,018,000 (compared with $412,569,000 as at 31 December 2011 (restated under IPSAS)). The end-of-service benefits are fully unfunded. However, UNRWA allocates funding each year equivalent to the cash payout for that particular year. The remaining funds will be allocated in future years on a similar basis.

15.4 In accordance with the requirements set out in International Public Sector Accounting Standard 25, the actuary has used the projected unit credit actuarial method to assess the plan's liabilities. Under this method, a "projected accrued benefit" is calculated for each benefit that will accrue for all active members of the plan. The projected accrued benefit is based on the plan's accrual formula and on the service period as at the valuation date but using a member's final compensation, projected to the age at which it is assumed that the employee will leave active service. The plan liability is the actuarial present value of the projected accrued benefits as at the valuation date for all active employees.

Normal and early retirement benefit

15.5 In the case of normal and early retirement, area staff are paid end-of-service benefits in accordance with rule 109.2 of the UNRWA area staff rules. The criteria and assumptions used in calculating normal and early retirement benefits according to the actuarial method under IPSAS include the following: (a) all area staff employees are eligible, and the normal retirement age is considered to be 60, plus a minimum service period of three years; (b) the amount payable is calculated on the basis of the formula of base salary times 11 per cent times number of completed years of service; (c) the service period is prorated until the last completed month of service; and (d) the base salary is the basic matrix salary without allowances. However, in Jordan, Lebanon and the Syrian Arab Republic, the basic matrix salary is adjusted for the fluctuation of the local currency against the United States dollar. In the West Bank, the basic matrix salary is adjusted for the fluctuation of the Jordanian dinar against the United States dollar.

15.6 The benefit referred to above is also payable in the case of early voluntary retirement. The conditions for early voluntary retirement are as follows: (a) the attainment of age 50 to 59, with 10 years of service or more; (b) a service period of 25 years or more; (c) the attainment of age 45 to 49, with a service period of 10 years or more; and (d) 20 to 24 years of service. The aforementioned eligibility criteria for early retirement are listed in descending order and are subject to an annual budget set by the Agency.

Termination in the interests of the Agency

15.7 Area staff are paid end-of-service benefits in accordance with rule 109.9 of the UNRWA area staff rules if the termination is as stipulated in rule 109.1 of the staff rules and is in the interests of the Agency as reflected in the following criteria: (a) the service period must be equal or greater than one year; (b) the employee is paid under either of the two schemes set out below, with the benefit amount and the application terms varying by years of qualified service and attained age:

Years of qualifying service	*Months of base salary*
0	0
1	1
2	1
3	2
4	3
5	4
6	5
7	6
8	7
9 or more	8

Age	*Months of base salary*
46	8.25
47	8.50
48	8.75
49	9.00
50	9.25
51	9.50
52	9.75
53	10.00
54	10.25
55	10.50

(c) the above benefit is not paid if separation from service is initiated by the employee (e.g., through resignation); (d) the service period is prorated until the last completed month of service; and (e) the base salary is the basic matrix salary without allowances. However, in Jordan, Lebanon and the Syrian Arab Republic, the basic matrix salary is adjusted for the fluctuation of the local currency against the United States dollar. In the West Bank, the basic matrix salary is adjusted for the fluctuation of the Jordanian dinar against the United States dollar.

Death benefits

15.8 Death benefits for area staff are paid in accordance with rule 109.8 of the UNRWA area staff rules. In the event of separation as a result of the death of an area staff member, the Agency shall pay a death benefit to the staff member's nominated beneficiary or beneficiaries. The death benefit shall be computed either: (a) as 11 per cent of the deceased staff member's ending annual salary and cost-of-living allowance (positive or negative) for each year of qualifying service, plus a supplemental benefit representing 50 per cent of ending annual salary and cost-of-living allowance (positive or negative); or (b) as 200 per cent of ending annual salary and cost-of-living allowance (positive or negative), whichever is greater.

Disability benefits

15.9 Area staff are paid in accordance with UNRWA area staff rule 109.7 if terminated on the stated ground that they are, for reasons of health, incapacitated for further service with the Agency. In the event of the disability of a staff member on or after 1 September 1987, and subject to paragraphs 3, 4, 5 and 6 of the above-mentioned rule, a disability benefit is computed either: (a) as 11 per cent of ending annual salary and cost-of-living allowance (positive or negative) for each year of qualifying service; or (b) as 200 per cent of ending annual salary and cost-of-living allowance (positive or negative), whichever is greater.

Reconciliation of end-of-service benefits

15.10 The interest costs and service costs incurred during the year have been directly accounted for in the statement of financial performance. The Agency introduced currency protection for the Jordan field in 2012. Although the Jordanian dinar is currently pegged against the United States dollar, the introduction of currency protection changes the liability into a United States dollar liability rather than a Jordanian dinar liability. Hence, the discount rate was changed from 6.5 per cent (which had been used in the previous valuation) to 4.75 per cent, which is used to discount United States dollar liabilities. This change was considered a benefit enhancement for Jordan local staff and has been directly accounted for in the statement of financial performance. The amount of interest costs, service costs and past service costs accounted for is shown in the table below.

15.11 International Public Sector Accounting Standard 25 allows the actuarial gains and losses that are within the corridor to be recognized outside the statement of financial performance and requires the presentation of the actuarial gains and losses in the statement of changes in net assets/equity. The amount of actuarial gains (losses) presented in the statement of changes in net assets/equity is $11,556,000.

15.12 Interest costs and service costs amounting to $51,112,000 and benefit enhancement due to the introduction of current enhancements in the Jordan field have been recognized in the statement of financial performance. The actuarial gains (losses) are directly accounted for in the statement of changes in net assets/equity in accordance with Standard 25. In the 2012 valuation of end-of-service liabilities, the actuaries determined actuarial losses to be $11,556,000. Accordingly, in the cash flow statement the actuarial losses were deducted rather than added, because they were directly accounted for in the statement of changes in net assets/equity.

(Thousands of United States dollars)

	31 December 2012
Opening balance as at 1 January 2012	412 569
Interest costs for 2012	20 760
Service costs for 2012	30 352
Past service costs[a]	16 447
Payments in 2012	(28 668)
Actuarial (gains)/losses	11 556
Total	**463 016**

[a] Benefit enhancement due to the introduction of currency protection in the field of Jordan.

Key assumptions

15.13 The discount rate used was based on the currency and the term of the underlying liabilities. Where the benefit offered by the Agency provided protection for the fluctuation of the local currency against the United States dollar, the benefit was assumed to be in United States dollars, and the applicable United States dollar discount rate was used. This has been the case for the fields of Lebanon, the West Bank and the Syrian Arab Republic.

15.14 The discount rates and future escalation used, by field and currency, are as follows:

(Percentage)

Field	*Currency*	*Currency protection*	*Discount rate*	*Future escalation*
Gaza	United States dollar	No	4.75	2.50
Gaza headquarters	United States dollar	No	4.75	2.50
Jordan	Jordanian dinar	Yes (Jordanian dinar/United States dollar)	4.75	2.50
Amman headquarters	Jordanian dinar	Yes (Jordanian dinar/United States dollar)	4.75	2.50
West Bank	Jordanian dinar	Yes (Jordanian dinar/United States dollar)	4.75	2.50
Lebanon	Lebanese pound	Yes (Lebanese pound/United States dollar)	4.75	2.50
Syrian Arab Republic	Syrian pound	Yes (Syrian pound/United States dollar)	4.75	2.50

15.15 The discount rates were set with reference to government bonds, high-quality corporate bonds and other instruments, depending on the currency, term and availability of such instruments for the currency under consideration.

Step increments

15.16 According to the current salary matrices of the Agency, step increments can be either an amount or a percentage. Subject to satisfactory performance, step increments are applied once a year for each employee until the employee reaches the maximum step level, which currently stands at 24.

Exchange rates as at 31 December 2012

15.17 The exchange rates used to convert local currencies to the United States dollar are based on the United Nations exchange rates as follows: United States dollar, 1.000; Jordanian dinar, 0.708; Lebanese pound, 1,492.537; Syrian pound, 63.251.

Resignation rates

15.18 It is assumed that plan members will resign at the following rates per annum according to their attained ages. The resignation rate for attained ages of less than 30 is 3 per cent; for 30-34, 2 per cent; for 35-39, 1.5 per cent; and for 40 and above, 0 per cent.

Early retirement rates

15.19 It is assumed that plan members will elect for early retirement according to the rates set out below.

(Percentage)

	Number of years since early retirement conditions have been satisfied			
Attained age	*0*	*1*	*2*	*3 +*
Less than 45	8.0	5.0	3.0	1.0
45-49	8.0	5.0	3.0	1.0
50-54	8.0	5.0	3.0	1.0
55-59	8.0	5.0	3.0	1.0
60 and above	100.0	100.0	100.0	100.0

15.20 For the field of Jordan and Amman headquarters, the assumed early retirement rates set out above were multiplied by 150 per cent.

Mortality

15.21 It is assumed that active members of the plan will experience in-service mortality in accordance with the 1996 United States Annuity 2000 mortality table for males and females.

Disability

15.22 It is assumed that disability cases will occur annually according to the probabilities set out below.

Disability rate (per thousand)

Age	*Male*	*Female*
Less than 45	0.50	0.75
45-54	1.00	1.50
55-60	1.50	2.25

International staff end-of-service liability

15.23 The separation costs of international staff funded from the regular budget of the United Nations (146 posts as at 31 December 2012) are borne by the regular budget, and no provision for these costs is made in the Agency's financial statements, as the liability will be borne by the United Nations. As a result, UNRWA has not disclosed after-service health insurance, repatriation grant or leave pay encashment in its financial statements. These liabilities relating to international staff should be included in the financial statements contained in the report of the Board of Auditors on the United Nations.

15.24 As a part of the implementation of IPSAS, UNRWA appointed an actuarial consultant to determine the employee liabilities for international staff members not funded from the United Nations regular budget. The value of liabilities for international staff not funded from the regular budget is summarized in the table below.

(Thousands of United States dollars)

Benefit	*31 December 2012*	*1 January 2012 (restated)*
Repatriation grant	565	597
Shipment	585	598
Travel	179	178
After-service health insurance	491	481
Outstanding annual leave	406	439
Total	**2 226**	**2 293**

Assumptions

15.25 The discount rate is assumed to be 4.75 per cent, and future escalation is assumed to be 3 per cent. The general inflation considered for travel and shipment costs is 2 per cent. The after-service health insurance premium applied for United States nationality only is 6 per cent, and that applied for other nationalities is 4 per cent. It is assumed that plan members will resign at the following rates per annum according to their attained ages: less than 30, 3 per cent; 30-34, 2 per cent; 35-39, 1.5 per cent; and 40 and above, 0 per cent. It is assumed that active members of the plan will experience in-service mortality in accordance with the 1996 United States Annuity 2000 mortality table for males and females.

15.26 After-service health insurance coverage is optional for eligible former international project staff members and their dependants. The Agency contribution to the after-service health insurance premium is set at 50 per cent, with the rest paid by the former staff member. Aetna rates were used for international staff members not funded from the United Nations regular budget and holding United States citizenship, while Vanbreda rates were used for other nationalities. It is of note that only three employees are expected to qualify for this benefit on the assumption of no contract extension.

Note 16
Other current liabilities

Other current liabilities comprise the following:

(Thousands of United States dollars)

	31 December 2012	*1 January 2012 (restated)*
Goods not paid for and not received	6 375	2 688
Other goods in transit liabilities	1 744	459
Donor refunding	1 324	–
Total	**9 443**	**3 147**

Note 17
Advance contribution

The amount of contributions received in advance of the criteria for revenue recognition being met is as follows:

(Thousands of United States dollars)

	31 December 2012	*1 January 2012 (restated)*
Received from Governments	19 998	109
Received from intergovernmental organizations	–	16 973
Total	**19 998**	**17 082**

Note 18
Contingent liabilities, contingent assets and operating lease commitments

Contingent liabilities

18.1 The Agency's contingent liabilities as at 31 December 2012, compiled by the Legal Department, arise broadly from two categories: those in connection with personnel matters in respect of significant claims, litigation or arbitration and those associated with contractual matters. Contractual matters relate mostly to claims pertaining to procurement/purchase orders, construction and claims from landlords from whom the Agency rents buildings.

18.2 A number of personnel appeals that could involve the payment of salary and entitlements or other damages were pending with the UNRWA Dispute Tribunal and the United Nations Appeals Tribunal. The contingent liabilities relating to these appeals amounted to approximately $1,042,000 as at 31 December 2012.

18.3 The contingent liabilities for commercial contracts amounted to approximately $183,454,000 as at 31 December 2012.

Contingent assets

18.4 The Agency's contingent assets represent pledges for which donor agreements have been signed but with respect to which the criteria for revenue recognition have not been met. The total amount of contingent assets outstanding as at 31 December 2012 was $242,462,000.

Operating lease commitments

18.5 Operating costs include lease payments in the amount of $3,026,000 recognized as operating lease expenses during the year. The amount includes minimum lease payments. No contingent rent payments were made.

18.6 The Agency holds principally cancellable operating leases. The operating lease agreements relate mainly to school premises, health centres, land and collective shelters for camps, field administrative offices and warehouses/distribution centres. The total of future minimum lease payments is as follows:

(Thousands of United States dollars)

Not later than one year	333
Later than one year and not later than five years	365
Later than five years	27
Total	**725**

18.7 Most of the operating lease agreements contain renewal clauses that enable the Organization to extend the terms of the leases at the end of the original terms. Some of the agreements have escalation clauses based on a fixed percentage increase, or a fixed amount increase, applied at prespecified intervals or dates in the future. No lease agreements contain purchase options.

18.8 The host Governments and some charitable organizations in the fields in which UNRWA operates provide the use of land for no or nominal rent to UNRWA for the benefit of Palestine refugees. The land is used to build schools, health centres or other UNRWA facilities that are administered by the Agency or in which it provides services.

18.9 These in-kind donations for the use of land have been valued at a fair value of $4,111,000 and are included in non-exchange revenue and occupancy costs. The fair value for these in-kind donations was calculated using recently negotiated commercial leases that UNRWA holds for land. The average rental return on the capital value of land for commercial leases was applied to the capital value of land, as assessed by external surveyors, that is provided to UNRWA at no or nominal value.

18.10 The Agency received revenue of $1,953,000 from sublease payments in 2012. All subleases are cancellable and contain no contingent lease payments.

Note 19
Revolving loan fund

19.1 Restricted contributions received for on-lending purposes are transferred to the revolving loan fund for both the Microfinance Department and the microcredit community support programme. The revolving loan fund is included as a component of the Microfinance Department and microcredit community support programme reserve in the statement of changes in net assets/equity.

19.2 The composition of the revolving loan fund as at 31 December 2012 was as follows:

(Thousands of United States dollars)

	31 December 2012	*1 January 2012*
Microfinance Department	23 424	23 305
Microcredit community support programme	2 332	2 333
Total	**25 756**	**25 638**

Note 20
Cash contributions revenue

Total cash contributions revenue by source received in 2012 was as follows:

(Thousands of United States dollars)

	Cash
Governments	655 773
Intergovernmental organizations	191 395
Non-governmental organizations and other entities	15 011
United Nations organizations	35 705
Total	**897 884**

Note 21
In-kind contributions revenue

Total in-kind contributions revenues by source received in 2012 was as follows:

(Thousands of United States dollars)

	In kind
Governments	18 997
Intergovernmental organizations	–
Non-governmental organizations and other entities	1 582
United Nations organizations	1 107
Total	**21 686**

Note 22
Interest on loans

Interest on loans represents interest charged on loans issued by the Microfinance Department and the microcredit community support programme throughout the five fields.

Note 23
Interest revenue

Interest revenue is recognized over the period during which it is earned. The amount of interest on bank deposits is $1,155,000.

Note 24
Currency exchange gain/(loss)

Currency exchange gains or losses are realized and unrealized exchange gains or losses on the translation of non-United States dollar-denominated balances and transactions during the year.

(Thousands of United States dollars)

Realized currency exchange rate gain	2 072
Unrealized currency exchange rate loss	(2 355)
Accounts receivable income realized exchange rate gain	2 214
Total	**1 931**

Note 25
Project support cost recovery

UNRWA is entitled to a specific percentage of the expenditures incurred on certain projects in accordance with donor agreements. Programme support cost recoveries are recognized as income and represent recoveries of overhead costs incurred by the Agency in implementing the related projects. The amount of programme support cost recovery is $167,000.

Note 26
Miscellaneous revenue

26.1 Miscellaneous revenue in 2012 comprised the following:

(Thousands of United States dollars)

Canteen lease revenue	1 953
Profit on income-producing activities	26
Sundries	295
Income received from United Nations agencies	265
Refunds to donors	(1 323)
Total	**1 216**

Refunds to donors represent amounts that have been recorded as revenue but are required to be refunded to donors in accordance with the terms of donor agreements.

Note 27
Wages, salaries and employee benefits

Wages, salaries and employee benefits in 2012 consisted of the following:

(Thousands of United States dollars)

International staff	38 236
Area staff	
Basic salaries, allowances and benefits	497 559
Area Staff Provident Fund contributions	49 692
Health-related expenses	5 902
Total	**591 389**

Note 28
Supplies and consumables

The composition of supplies and consumables in 2012 was as follows:

(Thousands of United States dollars)

Basic commodities	75 287
Clothing supplies	302
Fresh food	1 510
Medical supplies	23 255
Miscellaneous supplies	9 862
Sport supplies	175
Textbooks and library books	5 811
Transportation supplies	6 305
Total	**122 507**

Note 29
Occupancy, utilities and premises costs

Occupancy, utilities and premises costs in 2012 included the following:

(Thousands of United States dollars)

Rental of premises	7 491
Maintenance of premises	4 604
Utilities	5 777
Total	**17 872**

Note 30
Contracted services

The composition of services expense in 2012 was as follows:

(Thousands of United States dollars)

Construction and equipment	74 203
Contractual costs	20 790
Hospital costs	18 669
Miscellaneous, including accruals	8 644
Consultancy costs	11 786
Demurrage and port charges	4 838
Training costs	3 913
Travel	2 801
Total	**145 644**

Note 31
Subsidies

31.1 Subsidies represent amounts paid to Palestine refugees for the following:

(Thousands of United States dollars)

Cash subsidies to beneficiaries	61 255
Job creation programme	2 265
Patient subsidies	4 931
Subsidies for the construction and repair of shelters	13 963
Total	**82 414**

31.2 Cash subsidies paid to beneficiaries provide selective cash assistance for conflict-affected Palestine refugees in the Syrian Arab Republic, food security and rent subsidies.

Note 32
Segment reporting

32.1 A segment is a distinguishable activity or group of activities for which it is appropriate to separately report financial information. Segment information is provided on several bases to reflect UNRWA objectives and activities. Full segment reporting is provided for sources of funds segments. Segment expense reports are provided for (a) human development goals, (b) major programmes and (c) geographical locations.

(a) Sources of funds

32.2 A fund is an accounting entity established to account for transactions relating to a specified purpose or objective. Funds are segregated for the purpose of conducting specific activities or attaining certain objectives in accordance with special regulations, restrictions or limitations. The financial statements are prepared on a fund accounting basis, showing at the end of the period the consolidated position of all funds. Fund balances represent the accumulated residual of revenue and expenses.

32.3 UNRWA activities are financed through five fund groups. Each group of funds has differing parameters for utilization of the revenue.

32.4 The unearmarked fund is part of the UNRWA General Fund and is the principal means of financing the Agency’s recurrent activities. The fund enables the Agency to meet obligations from authorized appropriations and is financed primarily by voluntary contributions and in-kind donations from Governments, intergovernmental and non-governmental bodies and host authorities.

32.5 The earmarked fund is also part of the UNRWA General Fund, but the use of funds is restricted to specific activities (e.g., for direct support, cash and food assistance, through the social safety net programme) undertaken during a defined time period within a defined budget.

32.6 The Microfinance Department fund is used to provide credit for enterprise activities, household consumption and housing needs that will improve the quality of life of householders and small-business owners and will help sustain jobs, reduce poverty, empower women and provide income-generating opportunities for Palestine refugees.

32.7 Emergency appeal funds are used to address emergency needs through the delivery of emergency relief, for example, food aid, shelter and medical supplies. Funds are raised mainly through the Consolidated Appeals Process and are to be utilized during specified time periods.

32.8 Project funds are used to meet capital expenditure needs (e.g., school/health centre construction) or development needs to improve or supplement existing programmes and systems (e.g., environmental health improvement). Projects are undertaken to meet a specific objective, and contributions are time-bound and earmarked for the specified purpose(s).

(b) Human development goals

32.9 As part of its planning approach, UNRWA has five human development goals, to provide it with direction in fulfilling its mission of helping Palestine refugees. Fifteen strategic objectives that guide UNRWA core activities are consolidated into the five human development goals as follows:

- A long and healthy life, including the objectives of: (a) ensuring universal access to quality, comprehensive primary health care; (b) protecting and promoting family health; and (c) preventing and controlling diseases;
- Acquired knowledge and skills, including the objectives of: (a) ensuring universal access to and coverage of basic education; (b) enhancing education quality and outcomes against set standards; and (c) improving access to education opportunities for learners with special education needs;
- A decent standard of living, including the objectives of: (a) reducing abject poverty; (b) mitigating the effects of emergencies (both small-scale family and national crises) on individuals; (c) offering inclusive financial services and increased access to credit and savings facilities, especially for vulnerable groups such as women, youth and the poor; (d) improving employability; and (e) improving the urban environment through sustainable camp development and the upgrading of substandard infrastructure and accommodation;
- Human rights enjoyed to the fullest possible extent, including the objectives of: (a) ensuring that service delivery meets the protection needs of beneficiaries, including vulnerable groups; (b) safeguarding and advancing the rights of Palestine refugees by promoting respect for human rights, international humanitarian law and international refugee law; (c) strengthening the capacity of refugees to formulate and implement sustainable social services in their communities; and (d) ensuring that Palestine refugee registration and eligibility for UNRWA services are carried out in accordance with relevant international standards;
- Effective and efficient governance, including the objectives of providing overall direction and control of UNRWA and ensuring efficient operations and effective financial and risk management.

(c) Programme

32.10 UNRWA is functionally organized under five programmes that provide services to its beneficiaries or internal support services, as follows:

- The education programme provides basic and secondary education, education for learners with special education needs and vocational and technical training. The programme has 10 vocational training centres, which provide skills training in such fields as pharmacy, plumbing, carpentry, business and computing. The programme offers in-service training and development for teachers to develop their professional qualifications and pre-service training for new teachers. The programme also encourages students' progression to higher education through scholarships;

- The health programme provides a network of primary health-care facilities and mobile clinics that provide the foundation of its health services, offering preventive, general medicine and specialist care services tailored for each stage of life. Although the programme is focused mainly on primary health care, it also helps Palestine refugees to gain access to secondary and tertiary care services. The environmental health subprogramme controls the quality of drinking water, provides sanitation and carries out vector and rodent control in refugee camps;

- The infrastructure and camp improvement programme addresses the deteriorating living conditions of Palestine refugees in camps. The programme promotes environmentally and socially sustainable neighbourhoods. UNRWA repairs shelters and, in coordination with the host Governments, plans for rehousing and reconstruction projects after demolitions caused by armed conflict or other emergencies. The programme manages the construction and maintenance of all UNRWA facilities and installations, and also promotes a safe and healthful urban environment for Palestine refugees through the provision of well-maintained water, wastewater and storm-water drainage. It also maintains electricity infrastructure and accessible road and footpath networks;

- The relief and social services programme provides a range of direct and indirect social protection services for Palestine refugees. The relief services subprogramme provides social safety-net assistance that includes basic food support, cash subsidies and additional family income supplements for the most vulnerable Palestine refugees caught in the cycle of abject poverty. It also provides selective cash assistance, one-off cash grants for basic household needs in family emergencies. In addition, the subprogramme provides direct aid during emergencies caused by violence and political unrest, along with shelter rehabilitation in coordination with other programmes. The social services subprogramme promotes community-based action that enables particularly vulnerable refugees to become more self-reliant. The programme particularly addresses the needs of women, refugees with disabilities, young people and the elderly. It also helps vulnerable refugees through its microcredit programme, which is managed by community-based organizations;

- The support departments assist the Commissioner-General in the smooth running and governance of the Agency. This includes the effective management of personnel and financial resources, oversight, internal communication, legal support, fund-raising, advocacy and outreach to external interlocutors.

(d) Geographical locations

32.11 Although UNRWA goals and services are delivered primarily within a programme approach, the Agency's operations are managed on a field basis. UNRWA operates in five fields: Jordan, Lebanon, the Syrian Arab Republic and the occupied Palestinian territory (the West Bank, including East Jerusalem, and the Gaza Strip). Each field provides similar services but is distinctive to some extent, owing to the particular political, humanitarian and economic contexts in which the field operates and the status and rights of the Palestine refugees enjoyed in it.

32.12 The operations of the five field offices, which, together with UNRWA headquarters, provide services directly to Palestine refugees, are described below:

- *Gaza field office*. The Gaza Strip has a population of more than 1.5 million, including some 1.3 million registered Palestine refugees. The field office supports eight camps, 243 schools, two vocational and technical training centres, 21 primary health centres, six community rehabilitation centres and seven women's programme centres. The ongoing blockade of the Gaza Strip has severely affected the economy and the enjoyment of a range of human rights by Palestine refugees;

- *Lebanon field office*. Approximately 455,000 Palestine refugees are registered with UNRWA in Lebanon, with many living in refugee camps. The field office supports 12 camps, 68 schools, two vocational and technical training centres, 28 primary health centres, one community rehabilitation centre and nine women's programme centres. Palestine refugees in Lebanon do not enjoy several basic human rights; for example, they have restricted access to the local labour market;

- *Syrian Arab Republic field office*. UNRWA is mandated to provide services to more than 486,000 Palestine refugees living in the official camps and the three unofficial camps in the Syrian Arab Republic. The ongoing armed conflict in the Syrian Arab Republic has affected the economy, thus impacting the Palestine refugee community. The field office supports nine camps, 118 schools, the Damascus Training Centre, 23 primary health centres, five community rehabilitation centres and five women's programme centres. While Palestine refugees have many of the rights of Syrian citizens, including access to social services provided by the Government, development indicators reveal that they lag behind the host population in key areas;

- *Jordan field office*. More than 2 million Palestine refugees are registered in Jordan. The field office supports 10 camps, 172 schools, two vocational and technical training centres, 24 primary health centres, eight community rehabilitation centres and 12 women's programme centres. All Palestine refugees in Jordan have full citizenship with the exception of some 140,000 Palestine refugees originally from Gaza, who are eligible for temporary passports but are not entitled to vote or to work in government;

- *West Bank field office*. The West Bank covers 5,500 square kilometres, with an estimated population of 2.4 million. A quarter of the registered Palestine refugees live in 19 refugee camps, with most others living in West Bank towns and villages. The field office supports 19 camps, 98 schools, three vocational and technical training centres, 42 primary health centres, 15 community rehabilitation centres and 16 women's programme centres. West Bank refugees have been hard hit by closures imposed on the West Bank by the Israeli authorities, as historically they have been largely dependent on income from work inside Israel.

- *UNRWA headquarters*, whose functions are located in three locations: the Gaza Strip, East Jerusalem and Amman. The headquarters organization includes the Programme Coordination and Support Unit, the Administrative Support Department, the Department of Internal Oversight Services, the Human Resources Department, the Department of Legal Affairs, the Executive Office, the Finance Department, the Enterprise Resource Planning Department and the External Relations and Communication Department, as well as the education, health, relief and social services, infrastructure and camp improvement, and microfinance programme departments. The headquarters function also includes representative offices in New York, Washington, D.C., Geneva and Brussels and a liaison office in Cairo.

(e) Basis of pricing for inter-segment transfers and charges

32.13 Programme support costs are incurred by UNRWA in support of the implementation of its non-regular budget activities that cannot be directly attributed to specific activities, projects or programmes. Programme support costs represent administrative, managerial, logistical and other support costs, including costs relating to staff recruitment, budgetary and financial control, information and communications technology support, and actions in respect of procurement, transport and warehousing.

32.14 Programme support costs represent a recovery of project expenditures to ensure that non-regular activities do not constitute financial costs in terms of the Agency's regular budget.

32.15 Programme support costs, at a uniform standard rate of 11 per cent, are usually charged against all contributions for non-regular budget activities except for those of the Microfinance Department, with respect to which a standard rate of 6 per cent is charged on the Department's running costs, excluding staff costs.

Segment reporting by fund: financial position as at 31 December 2012

(Thousands of United States dollars)

	Unearmarke activitie	*Earmarked activities*					
	General Fund	*Restricted funds*	*Microfinance Department*	*Emergency appeals*	*Projects*	*Inter-fund balances*	***Total***
Assets							
Current assets							
Cash and cash equivalents	7 625	7 355	9 268	32 070	176 115		**232 433**
Short-term loans receivable			18 256		1 165		**19 421**
Contributions receivable	824	2 364	352	7 642	11 971	(352)	**22 801**
Accounts receivable	50 040	9			506		**50 555**
Other current assets	2 469	23	486	392	607		**3 977**
Operational Microfinance Department account with UNRWA		480				(480)	
Inventories	29 413	219					**29 632**
Non-current assets							
Other non-current assets	354						**354**
Long-term loans receivable			1 871		806		**2 677**
Property, plant and equipment	394 900	6 448	896	2 424	33 104		**437 772**
Intangible assets	5 381	1 188	305				**6 874**
Total assets	**491 006**	**18 086**	**31 434**	**42 528**	**224 274**	**(832)**	**806 496**
Liabilities							
Current liabilities							
Payables and accruals	33 810	1 700	531	9 082	16 892		**62 015**
Employee benefits	61 802	237	412	771	426		**63 648**
Operational Microfinance Department account with UNRWA			480			(480)	
Other current liabilities	9 443						**9 443**
Advance contributions	16 172			50	3 776		**19 998**
Non-current liabilities							
Employee benefits	431 075	84	2 275	52	85		**433 571**
Other non-current liabilities	1		9 875	50	1 262		**11 188**
Total liabilities	**552 303**	**2 021**	**13 573**	**10 005**	**22 441**	**(480)**	**599 863**
Net assets	**(61 297)**	**16 065**	**17 861**	**32 523**	**201 833**	**(352)**	**206 633**
Net assets/equity							
Other reserves	(11 555)						**(11 555)**
Capital reserve: microcredit community support programme and Microfinance Department			23 424		2 332		**25 756**
Accumulated surplus/deficit	(49 742)	16 065	(5 563)	32 523	199 501	(352)	**192 432**
Total net assets/equity	**(61 297)**	**16 065**	**17 861**	**32 523**	**201 833**	**(352)**	**206 633**

Segment reporting by fund: financial performance as at 31 December 2012

(Thousands of United States dollars)

	Unearmarked activities	*Earmarked activities*					
	General Fund	*Restricted funds*	*Microfinance Department*	*Emergency appeals*	*Projects*	*Inter-fund balances*	***Total***
Revenue							
Cash contributions	544 074	20 915	352	160 346	172 549	(352)	**897 884**
In-kind contributions		11 943		6 826	2 917		**21 686**
Interest on loans			8 870				**8 870**
Interest on bank deposits	843		60		252		**1 155**
Other revenue							
Foreign currency exchange gain	2 475	759	(951)	(69)	(283)		**1 931**
Programme support cost recovery	21 778					(21 611)	**167**
Financial derivative gain/loss	11 232						**11 232**
Miscellaneous revenue	6 574	(849)	(570)	(2 605)	(1 334)		**1 216**
Total revenue	**586 976**	**32 768**	**7 761**	**164 498**	**174 101**	**(21 963)**	**944 141**
Expenses							
Wages, salaries and employee benefits	536 826	7 668	5 912	30 635	15 800	(5 452)	**591 389**
Supplies and consumables	35 876	28 895	116	51 932	5 779	(91)	**122 507**
Occupancy, utilities and premises costs	10 039	5 740	457	710	967	(41)	**17 872**
Contracted services	30 811	876	1 370	50 503	56 316	5 768	**145 644**
Programme support costs		46		11 718	9 847	(21 611)	
Cash subsidies	18 845	2 930		22 194	3 856	(115)	**82 414**
Depreciation	22 667		266				**22 933**
Provisions	6 874		2 105	(971)	(1 276)		**6 732**
Loss on disposal	1 422						**1 422**
Impairment of property, plant and equipment	679						**679**
Total expenses	**664 039**	**46 155**	**10 226**	**166 721**	**125 993**	**(21 542)**	**991 592**
Surplus/(deficit) for the year	**(77 063)**	**(13 387)**	**(2 465)**	**(2 223)**	**48 108**	**(421)**	**(47 451)**

Segment reporting by human development goal: expenses as at 31 December 2012

(Thousands of United States dollars)

	Long and healthy life	*Acquired knowledge and skills*	*Decent standard of living*	*Human rights enjoyed to the fullest*	*Effective and efficient governance and support in UNRWA*	*Unallocated human development goal*	*Inter-fund balances*	***Total***
Wages, salaries and employee benefits	79 600	349 164	53 280	9 250	104 954	593	(5 452)	**591 389**
Supplies and consumables	23 574	9 768	81 862	343	6 615	436	(91)	**122 507**
Occupancy, utilities and premises costs	1 473	4 762	2 507	334	8 742	95	(41)	**17 872**
Contracted services	21 807	18 990	29 167	2 230	20 493	47 189	5 768	**145 644**
Programme support costs						21 611	(21 611)	
Cash subsidies	5 355	153	70 547	2 200	1 310	2 964	(115)	**82 414**
Depreciation	3 151	11 999	2 694	1 048	4 041			**22 933**
Provisions		809	–	1 176	4 747			**6 732**
Loss on disposal	313	646	53	8	386	16		**1 422**
Impairment of property, plant and equipment	71	490	25		93			**679**
Total	**135 344**	**396 781**	**240 135**	**16 589**	**151 381**	**72 904**	**(21 542)**	**991 592**

Segment reporting by programme: expenses as at 31 December 2012

(Thousands of United States dollars)

	Education	*Health*	*Infrastructure and camp development*	*Relief and social services*	*Support departments*	*Inter-fund balances*	***Total***
Wages, salaries and employee benefits	358 849	74 537	32 753	28 391	102 311	(5 452)	**591 389**
Supplies and consumables	11 785	24 344	5 889	77 492	3 088	(91)	**122 507**
Occupancy, utilities and premises costs	5 840	1 409	1 538	1 307	7 819	(41)	**17 872**
Contracted services	20 330	32 532	32 413	32 470	22 131	5 768	**145 644**
Programme support costs	4 800	1 712	5 979	3 813	5 307	(21 611)	
Cash subsidies	1 980	5 493	2 136	55 510	17 410	(115)	**82 414**
Depreciation	13 956	2 858	2 748	1 665	1 706		**22 933**
Provisions				1 986	4 746		**6 732**
Loss on disposal	646	328	264	62	122		**1 422**
Impairment of property, plant and equipment	493	71	82	19	14		**679**
Total	**418 679**	**143 284**	**83 802**	**202 715**	**164 654**	**(21 542)**	**991 592**

Segment reporting by geographical location: financial performance as at 31 December 2012
(Thousands of United States dollars)

	Gaza field	*Lebanon field*	*Syria Arab Republic field*	*Jordan field*	*West Bank field*	*Headquarters*	*Inter-fund balances*	***Total***
Expenses								
Wages, salaries and employee benefits	233 498	67 353	51 029	112 823	99 239	32 899	(5 452)	**591 389**
Supplies and consumables	79 255	11 077	6 068	13 314	12 321	563	(91)	**122 507**
Occupancy, utilities and premises costs	3 733	2 301	1 523	5 114	4 652	590	(41)	**17 872**
Contracted services	67 147	44 720	3 570	2 617	9 956	11 866	5 768	**145 644**
Programme support costs	13 333	3 107	1 382	244	3 323	222	(21 611)	
Cash subsidies	29 178	15 444	12 899	4 811	19 050	1 147	(115)	**82 414**
Depreciation	11 295	2 653	1 757	2 604	4 196	428		**22 933**
Provisions	64	15	1 186	316	737	4 414		**6 732**
Loss on disposal	1 168	36	217		1			**1 422**
Impairment of property, plant and equipment	313		366					**679**
Total	**438 984**	**146 706**	**79 997**	**141 843**	**153 475**	**52 129**	**(21 542)**	**991 592**

Note 33
Presentation of budget information

33.1 As required under International Public Sector Accounting Standard 24, the actual amounts presented on a comparable basis with the budget shall, where the financial statements and the budget are not prepared on a comparable basis, be reconciled with the actual amounts presented in the financial statements, identifying separately any basis, timing and entity differences. There may also be differences in formats and classification schemes adopted for the presentation of financial statements and the budget.

33.2 UNRWA budget figures are determined on a modified cash basis (i.e., United Nations system accounting standards) and disclosed in the statement of comparison of budget and actual amounts (statement V) as the original budget derived from the 2012-2013 programme budget (Blue Book), as recommended by the Advisory Committee on Administrative and Budgetary Questions and endorsed by the General Assembly.

33.3 As compared with the Blue Book Budget, the General Fund budget, made available at the beginning of each year, reflects reduced requirements based on the end-of-year income forecast. However, for the projects budget, the resources are made available when contributions are received and/or, on exceptional basis, when funds are confirmed by donors for approved projects and through advances from the advance financing facility.

33.4 With the adoption of IPSAS, UNRWA has internally moved from a United Nations system accounting standards budget to an IPSAS budget (accrual budget). Hence, the final budget in financial statement V refers to an IPSAS budget and is used for comparison with the actual amounts.

33.5 The UNRWA budget encompasses three main entities (fund types): the General Fund unearmarked budget, funded mainly by voluntary contributions along with 146 international staff funded through the United Nations regular budget from assessed contributions; General Fund in-kind donations; and the projects budget.

33.6 The Agency’s budget structure follows a results-based budgeting format, as reflected in the two-year field implementation and headquarters department implementation plans, which are derived from the medium-term strategy for the period 2010-2015. The approved budget is also presented using classifications based on the nature of revenue and expenses.

33.7 The statement of financial position, the statement of financial performance, the statement of changes in net assets/equity and the statement of cash flow are prepared on a full accrual basis, using classifications based on the nature of revenue and expenses reflected in the statement of financial performance. The statement of comparison of budget and actual amounts (statement V) is prepared on an accrual accounting basis.

33.8 Basis differences occur when the approved final budget is prepared on a basis other than the accounting basis on which the financial statements are prepared. As the approved budget and the financial statements for UNRWA are prepared on an accrual basis, there are no basis differences.

33.9 Timing differences occur when the budget period differs from the reporting period reflected in the financial statements. The biennial budget for 2012-2013 provides a breakdown of the budget by year for purposes of comparison against actual amounts. There are no timing differences for UNRWA for purposes of the comparison of budget and actual amounts.

33.10 Entity differences occur when the budget omits programmes or entities that are part of the entity for which the financial statements are prepared. Entity differences occur as the approved budget, as noted above, includes the General Fund unearmarked budget, General Fund in-kind donations and the projects budget. The financial statements also include the emergency appeals fund, the Microfinance Department fund and the earmarked fund of the General Fund.

33.11 Reconciliations between (a) the actual amounts on a comparable basis in the statement of comparison of budget and actual amounts (statement V) and the actual amounts in the statement of cash flow (statement IV) and (b) the actual amounts on a comparable basis in the statement of comparison of budget and actual amounts (statement V) and the total revenue and total expenses actual amounts in the statement of financial performance (statement II) for the period ended 31 December 2012 are presented below.

(Thousands of United States dollars)

	Operating	*Investing*	*Financing*	*Total*
Actual amounts on a comparable basis (statement V)	(19 108)	–	–	(19 108)
Basis differences	–	–	–	–
Timing differences	–	–	–	–
Entity differences	(14 280)	(4 310)	118	(18 472)
Actual amounts in the statement of cash flow (statement IV)	**(33 388)**	**(4 310)**	**118**	**(37 580)**

(Thousands of United States dollars)

	Total revenues	*Total expenses*
Actual amounts on a comparable basis (statement V)	761 077	780 185
Basis differences	–	–
Timing differences	–	–
Entity differences	183 064	211 407
Actual amounts in the statement of financial performance (statement II)	**944 141**	**991 592**

Explanations of material differences

33.12 Explanations of material differences between the original budget and the final budget, as well as between the final budget and the actual amounts, are presented below.

Original and final budgets (income and expense/capital expenditure)

33.13 The **original income** of the General Fund budget is the projected income as reflected in the Blue Book, which for 2012 was $521.7 million. As for the General Fund in-kind donations and projects budgets, original income is equivalent to the budgeted figures reflected in the Blue Book on the assumption that all will be funded.

33.14 The **final income** of the General Fund budget is the actual income received, while for the General Fund in-kind donations and projects budgets, final income is equivalent to the total budget allocation at year-end.

33.15 The **original budget of expenses/expenditure** is the budget as published in the Blue Book, while the **final budget of expenses/expenditure** is the approved 2012 budget allocation at year-end.

33.16 The 2012 programme budget, as reflected in the Blue Book for 2012-2013, was $1,013.8 million (United Nations System Accounting Standards view). This is disclosed in financial statement V as “original budget”. In compliance with IPSAS, the final 2012 programme budget (accrual budget) was $1,044.9 million, reflecting an increase of $31.1 million, or 3.1 per cent. This is disclosed in financial statement V as “final budget”. The $31.1 million is a reflection of the increase in the final budget for each entity as follows: an increase in the General Fund budget by $5.7 million, due to IPSAS changes and reductions in other costs; an increase in the projects budget by $18.2 million, reflecting the additional needs in the Gaza, Lebanon and Syrian Arab Republic field offices; and an increase in General Fund in-kind donations by $7.2 million. The following are the main basic changes that occurred as UNRWA moved from the United Nations system accounting standards to IPSAS with respect to the General Fund budget:

$653.1 million	**2012 original budget — General Fund budget**
+$44.9 million	**Severance provision** (recorded monthly as an expense on the statement of financial performance — non-cash item)
+$20.4 million	**Depreciation** (net increase in depreciation of property plant and equipment)
-$2.7 million	**Capital** (transfer from expenditure to capital expenditure)
-$6.6 million	**Early voluntary retirement** (no longer reported on the statement of financial performance; it is a statement of financial position item)
-$13.1 million	**Retirement benefits** (taken upon retirement; no longer reported on the statement of financial performance; under IPSAS statement of financial position)
-$13.0 million	**Enterprise resource programme** (is capital in nature and an intangible asset; hence, transfer from expenditure to capital expenditure).
-$9.2 million	**Net redeployments — budget hearing results**
$673.8 million	**1 January 2012 IPSAS budget — core General Fund budget**
+$10.3 million	Supplies and consumables (food — redeployment through the year)
+$3.4 million	Cash subsidies — redeployment through the year
-$1.0 million	Contracted services — redeployment through the year
-$0.8 million	Equipment and construction — redeployment through the year
-$39.8 million	Provision — decrease in end-of-year forecast and redeployment through the year
$645.9 million	**31 December 2012 IPSAS final budget — General Fund expense budget**
+$12.9 million	**31 December 2012 IPSAS final budget — General Fund capital budget**
+$658.9 million	**31 December 2012 IPSAS final budget — General Fund expense and capital expenditure**
+$377.0 million	**31 December 2012 projects budget**
+$9.0 million	**31 December 2012 in-kind donations budget**
$1,044.9 million	**31 December 2012 total final budget**

Utilization of the budget

33.17 The variation in the budgetary utilization of the different budget cost components is due to various factors such as salary increase, increase in severance provision (IPSAS adjustment), depreciation provision (IPSAS adjustment), and purchase orders and the relevant hard commitments not reflected in the actual amounts (IPSAS adjustment). The utilization rate against the various cost components rates is outlined below:

- Wages, salaries and employee benefits: 102 per cent, owing to increase in severance provision;
- Supplies and consumables: 75 per cent, owing to unliquidated purchase orders;
- Occupancy, utilities and premises costs: 112 per cent, owing to high costs;
- Contracted services: 43 per cent, owing to unliquidated service contracts at year-end;
- Cash subsidies: 75 per cent, owing to timing differences for cash subsidies to be funded from projects;
- Depreciation and amortization: 105 per cent, owing to additional assets capitalized during the year, not included in the budget.

Note 34
Going concern

34.1 The accompanying financial statements have been prepared under the assumption that the Agency will continue to operate as a going concern. As shown in the financial statements, however, the Agency incurred a net loss of $47,451,000 in 2012. This may raise doubt about the Agency's ability to continue as a going concern. The following factors provide evidence as to the continuing nature of the Agency as a going concern.

34.2 The Agency has total net assets of $206,633,000, and total current assets exceed total current liabilities by $203,715,000. The balance of cash and cash equivalents held by the Agency as at 31 December 2012 was $232,433,000. In addition, as described in note 18, at 31 December 2012 the Agency had contingent assets in the amount of $242,462,000, which related to contributions from donors for which the agreements had been signed but the criteria for revenue recognition had not yet been met.

34.3 UNRWA is funded by voluntary contributions from Member States and other donors for the support of its ongoing programmes and activities. All key donors reaffirm their support every six months at a semi-annual Advisory Commission meeting. Furthermore, UNRWA is actively diversifying its funding base by successfully targeting and increasing donations from emerging markets, such as the Middle East. As at 1 January 2012, the Agency had established a new Partnerships Unit, which has had successful discussions with high-net-worth philanthropic organizations.

34.4 Given the history of the Agency and the continuous efforts of management to mobilize resources for its operations, there is no threat to the Agency's short-term ability to operate as a going concern.

34.5 In 2013, as part of a strategic, medium-term approach, UNRWA will begin to develop its next medium-term strategy. The aim of the medium-term strategy is to provide the strategic framework for the Agency's operations for the period 2016-2021.

34.6 Funding the operations of the unearmarked activities of the General Fund has presented the greatest challenge to the Agency in recent years. As reflected in the segment reporting by fund, unearmarked activities incurred a deficit of $77,063 for 2012, and as at 31 December 2012 the net assets of the fund reflected a net deficit of $61,297. The Agency is actively seeking contributions to support its unearmarked activities in order to sustain core operations.

Note 35
Related parties

Related parties for UNRWA include:

(a) The Area Staff Provident Fund, as it is controlled by the Agency;

(b) The United Nations Secretariat, since it exercises significant influence over UNRWA, including because the salaries, related expenditures and liabilities of the majority of the Agency's international staff, including its key management personnel, are paid from the regular budget of the United Nations;

(c) Key management personnel, which include the members of the Management Committee, as they have authority with respect to planning, directing and controlling the activities of the Agency (or significant parts thereof). The major classes of key management personnel are (a) Commissioner-General/Deputy Commissioner-General and (b) field/headquarters Directors. The aggregate remuneration paid to key management personnel includes net salaries, post adjustment, entitlements such as allowances, grants and subsidies, and employer pension and health insurance contributions. Key management personnel remuneration incorporates housing allowances and representation allowances paid as part of salaries, despite the presence of a representative aspect to these allowances. Transactions conducted with key management personnel in 2012 are summarized as follows:

(Thousands of United States dollars)

	Number of individuals	*Total remuneration*	*Outstanding advances against entitlements*	*Outstanding loans*
Key management personnel	24	5 118	223	–

(d) No close family members of key management personnel were employed by the Agency during the year;

(e) Advances are those made against entitlements in accordance with UNRWA area and international staff rules and regulations. Advances against entitlements are widely available to all UNRWA staff.

Note 36
Subsequent events

Area staff retirement age

36.1 In 2013, the Agency increased the retirement age for area staff on an optional basis from 60 to 62, effective 1 January 2014. The change is expected to result in an increase in the respective employee benefit costs.

Ongoing conflict in the Syrian Arab Republic

36.2 While the destabilizing aspects of the so-called Arab Spring has so far bypassed Palestine and had limited political impact in Jordan, in the Syrian Arab Republic it had developed from limited demonstrations and protests in early 2011 into a full-scale armed conflict by June 2012. The ongoing conflict in the Syrian Arab Republic has affected the economy and the stability of the region. The consequent decrease in the value of the Syrian pound, increase in the costs of basic commodities, ongoing conflict, and physical damage to Agency assets have impacted UNRWA operations in the region. The conflict has continued into 2013, with no indication of a final resolution.

Note 37
Date and approval

The financial statements and notes were certified as correct by the Director of Finance and approved by the Commissioner-General and were issued on 31 March 2013.

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