Palestine for Credit & Development - FATEN
Ramallah – Palestine

Auditors' Report &
Financial Statements
for the year ended December 31, 2006

Talal Abu-Ghazaleh & Co.
Certified Public Accountants

Palestine for Credit & Development - FATEN
Ramallah – Palestine

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Auditors' Report

To the Shareholders
Palestine for Credit and Development (FATEN)
Ramallah – Palestine

We have audited the accompanying financial statements of **Palestine for Credit and Development (FATEN)**, which comprise the statement of financial position as at December 31, 2006 and the statement of activities, cash flows statement and statement of changes in shareholders' equity for the year then ended, and a summary of significant accounting polices and other explanatory notes.

Management responsibility for financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reposting Standards. This responsibility includes: designing, implementing and maintaining internal control 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.

Auditor's responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control 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 control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating 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.

Auditor's opinion

In our opinion, the financial statements give a true and fair view of financial position of the **Palestine for Credit and Development (FATEN)** as at December 31, 2006 and of its financial performance and its cash flows for the year then ended, in conformity with International Financial Reporting Standards.

Without qualifying our opinion, we draw attention to Note (2- a & c) to the financial statements. FATEN has changed the method of estimation of the provision for doubtful debts to be 8% of the outstanding portfolio except NGO and staff loans.

Talal Abu-Ghazaleh & Co.

Jamal Milhem
Certified Accountant License # (100/98)
Ramallah, February 24, 2007

Palestine for Credit & Development (FATEN)
Ramallah – Palestine
Statement of financial position as at December 31, 2006 ***Exhibit "A"***

	Note	2006	2005
Assets		**USD**	**USD**
Cash in hand and at banks	(3)	5,680,023	2,118,523
Net Loan Portfolio	(2b-c, 4a)	7,654,367	8,668,356
Other current assets	(5)	85,085	532,031
Fixed assets - net	(2d, 6)	396,520	364,892
Total assets		**13,815,995**	**11,683,802**
Liabilities and equity			
Payables and accruals	(7)	667,233	669,939
Long term loans	(8)	200,000	200,000
Provisions for employees' indemnity	(9)	720,645	619,763
Total liabilities		**1,587,878**	**1,489,702**
Equity			
Paid-in capital		4,080	4,080
Accumulated donations	(11)	14,381,038	12,233,519
Accumulated losses		(2,157,001)	(2,043,499)
Total equity		**12,228,117**	**10,194,100**
Total liabilities and Equity		**13,815,995**	**11,683,802**

"The accompanying notes constitute an integral part of this statement"

Palestine for Credit & Development (FATEN)
Ramallah – Palestine
Statement of income for the year ended December 31, 2006 ***Exhibit "B"***

	Note	2006 USD	2005 USD
Revenues			
Interest on loans		939,324	875,102
Profit on Morabaha		46,910	15,387
Commission revenues		7,542	11,216
Fees on loans		59,672	160,463
Provision for loan losses	(4)	(364,000)	(192,455)
Net interest income		**689,448**	**869,713**
Other operating revenues			
Collection of loans previously written-off		8,663	20,765
Application fees		8,425	14,407
Penalty fees and others		2,680	4,675
Bank interests		86,659	24,034
Consulting and MIS sales		8,375	10,700
Other revenues		7,422	8,374
Total other operating revenues		**122,224**	**82,955**
Total operating revenues		**811,672**	**952,668**
Operating and administrative expenses	(10)	(934,828)	(969,861)
Prior years adjustments		9,654	--
Net operating loss		**(113,502)**	**(17,193)**
Grants to subsidies operations	(11)	174,268	84,556
Net profit after grants		**60,766**	**67,363**

"The accompanying notes constitute an integral part of this statement"

Palestine for Credit & Development (FATEN)
Ramallah – Palestine
Statement of changes in equity for the year ended December 31, 2006 ***Exhibit "C"***

Description	Paid in capital USD	Accumulated donations USD	Accumulated losses USD	Total USD
Balance as at 01/01/2006	4,080	12,233,519	(2,043,499)	10,194,100
Donations recorded directly to balance sheet	--	1,973,251	--	1,973,251
Grants to subsidies operations	--	174,268	--	174,268
Net operating loss for the year	--	--	(113,502)	(113,502)
Balance as at 31/12/2006	**4,080**	**14,381,038**	**(2,157,001)**	**12,228,117**
	======	========	========	========
Balance as at 01/01/2005	4,080	7,809,701	(2,026,306)	5,787,475
Donations recorded directly to balance sheet	--	4,339,262	--	4,339,262
Grants to subsidies operations	--	84,556	--	84,556
Net operating loss for the year	--	--	(17,193)	(17,193)
Balance as at 31/12/ 2005	**4,080**	**12,233,519**	**(2,043,499)**	**10,194,100**
	=======	========	========	========

"The accompanying notes constitute an integral part of this statement"

Palestine for Credit & Development (FATEN)
Ramallah – Palestine
Cash flows statement for the year ended December 31, 2006 *Exhibit "D"*

Operating activities	Note	2006 USD	2005 USD
Net operating loss		(113,502)	(17,193)
Adjustments to reconcile changes in net assets during the year to net cash used for (provided from) activities			
Non cash items			
Depreciation expenses	(6)	37,308	44,258
Provision for loan losses	(4d)	364,000	192,455
Written-off loans	(4d)	--	(86)
Provision for employees' indemnity	(9)	164,435	137,541
Changes in current assets and current liabilities:			
Decrease (increase) in other current assets		446,946	(291,070)
Net (decrease) increase in loan portfolio		649,989	(6,560,266)
Decrease (increase) in payable and accruals		(2,706)	570,838
Employees' indemnity paid	(9)	(63,553)	(45,859)
Net cash flows provided from (used by) operating activities		**1,482,917**	**(5,969,382)**
Cash flows from investing activities:			
Purchase of fixed assets	(6)	(70,420)	(27,261)
Sold of fixed assets		1,484	--
Net cash used by investing activities		**(68,936)**	**(27,261)**
Cash flows from financing activities			
Donations and grants	(11)	2,147,519	4,423,818
Long term loans	(8)	--	200,000
Net cash provided from financing activities		**2,147,519**	**4,623,818**
Increase (decrease) in cash and cash equivalent		3,561,500	(1,372,825)
Cash and cash equivalent – beginning of year	(3)	2,118,523	3,491,348
Cash and cash equivalent – ending of year	**(3)**	**5,680,023**	**2,118,523**

"The accompanying notes constitute an integral part of these financial statements"

Palestine for Credit & Development (FATEN)
Ramallah – Palestine
Notes to the financial statements

1. Background:

a. Palestine for Credit and Development (FATEN) was part of Save the Children Federation – West Bank and Gaza. On July 14, 1998, FATEN was registered as a Private limited liability not for Profit Corporation in Gaza under registration number 563124478 in accordance with the Companies' Law of 1929. FATEN has commenced its operations on March 1, 1999. FATEN's authorized share capital is 10,000 common shares at par value USD 1 each. As of the financial statements date, the issued and fully paid capital amounted to USD 4,080.

The governmental controlling party is the Ministry of Economic.

The main objectives of FATEN are the following:

- Providing Palestinian micro-entrepreneurs with sustainable access to financial services.
- Offering diverse credit products and other financial services.
- Achieving qualitative and effective capacity and clients' services.
- Becoming financially sustainable institution.

FATEN employed 63 and 66 employees' as at December 31, 2006 and 2005 respectively.

These financial statements were approved by the board of directors on March 18, 2007.

2. Significant accounting policies:

a. Basis of preparation:

The financial statements have been prepared under the historical cost convention, in accordance with International Financial Reporting Standards, as published by the International Accounting Standards Boards (IASB), except for interest on group loans, which are accounted for when received, rather than when earned.

Loan status	**Provision percentage**
1-30 days overdue	10%
31-60 days overdue	50%
61-90 days overdue	75%
91-180 days overdue	100%

b. Use of Estimates:

The preparation of the financial statements in conformity with International Financial Reporting Standards requires management to make estimates and assumptions that affect reported assets and liabilities as well as reported income and expenses for each year. A material estimate that is particularly susceptible to significant changes relates to the determination of provisions for loan losses.

c. Loans receivable:

1. Loans are reduced by the provision for loan losses. Management evaluation the adequacy of the provision for loan losses regularly. Factors considered in evaluating the adequacy of the provision include the size of the portfolio, previous loss experience, current economic conditions and their effect on clients, and the performance of individual loans in relation to contract terms. The provision for loan losses charged to expenses is based on management's judgment of the amount necessary to maintain the allowance at a level adequate to absorb losses.

Management provides for loan losses every month in order to maintain the provision for loans is determined by applying defined percentages to the outstanding balances in various aging categories as shown in Note (2, a).

2. FATEN used this policy until Dec 31, 2005, and then it changed this policy to be calculated as at 8% percent for outstanding portfolio, Except NGOS and Employee loans.
3. FATEN was not a licensed financial intermediary, therefore; its provision policy is based on management's analysis of the historical performance of the overdue portfolio, age by the same categories rather than on Palestine Monetary Authority Regulation.

Written of loans are charged against the provision for loan losses when management believe that the principal is unlikely to be collected.

d. Types of Loans and guarantee:

These items consists the types of loans:

- Performance loans: the group guarantees
- Individual, Individual 11, Morabaha, Housing and Family guarantee: is salary transfer and sponsor person.
- NGOs and its staff loan the guarantee as provision for employees' indemnity and Provident fund.

e. Fixed assets:

Fixed assets are stated at cost on the date of acquisition or, in the case of gifts, at fair market value at date of donation. Depreciation is computed on a straight-line basis over the useful lives of the property and equipment using the following annual depreciation rates:

- Building	2%
- Vehicles	15%
- Furniture and equipment	15%

The carrying values of property and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets are written down to their recoverable mount.

f. Interest Revenues:

- FATEN used accrual basis to calculate the credit interest for all loans, and then calculated the interest rate as time average basis after take the amount of balance and interest. Except performing loans, because it is less than six months, so the interest will be smaller. After three months of accrued installment payment, no interests will be calculating for individual loans.
- There are no policies to rescheduling loan.

g. Donations:

- Donations to subsidize operating and administrative expenses are recorded in the statement of income as grant income.
- Donations to finance lending operations or the purchase of fixed assets are shown as direct additions to equity and the corresponding asset account.
- There are no in-kind donations during the year of 2006.

h. Expenses recognition:

Expenses are recognized when incurred based on the accrual basis of accounting.

i. Employees indemnity:

FATEN provides for employees' end of service benefits by accruing for one-month compensation for each year of service based on the last salary paid during the year, in accordance with labor law prevailing in Palestine. FATEN also provides employees a provident fund. Total contributions by the employees and FATEN are set at 10%, each based on the employees' basic monthly salaries.

j. Foreign currency transactions:

The books of accounts are maintained in Jordanian Dinars (JD). Transactions which are denominated in other currencies are converted into JD using the prevailing exchange rates at the date of the transactions.

Assets and liabilities, which are denominated in foreign currencies at the balance sheet date, are translated into JD using the prevailing exchange rates at the balance date. Exchange differences arising from these translations are recorded in the statement of income.

Exchange rates against JD as of the balance sheet date were as follows:

	2005	2006
	JD	JD
- USD	0.71	0.71
- NIS	0.15	0.168

k. Transaction to the reporting currency:

For the purpose of reporting to donors and other foreign interested parties, FATEN uses the USD as its reporting currency. Balances of assets and liabilities are translated into USD using the exchange rates prevailing at the balance sheet date. All income and expenses balances are translated to USD using the average rate of exchange prevailing during the year.

3. Cash in hand and at banks:

a. This item consists of:	2006	2005
	USD	USD
- Cash in hand	1,539	1,417
- Cash at banks- NIS	9,319	10,095
- Cash at banks – JD	185,252	213,989
- Cash at banks - USD	189,404	825,589
- Deposit at bank - b	4,735,428	610,984
Total	5,120,942	1,662,074
Deposits restricted for employees' Indemnity - b	559,081	456,449
Total	**5,680,023**	**2,118,523**
	========	========

b. Bank deposits at local banks in Palestine are short term in nature, with an average interest rate of 3.5% - 4.65% for deposits in USD.

c. **Description:**	Cash at bank		
	West Bank	Gaza	Total
	USD	USD	USD
- Current Accounts	310,919	73,056	383,975
- Deposit maturity /month or less	1,228,089	--	1,228,089
- Deposit maturity 1 month to 3 months	3,184,130	882,291	4,066,421
	4,723,138	**955,347**	**5,678,485**
	=======	=======	========

4. Net loan portfolio:

a. By type of loans:

	2006 USD	2005 USD
- Housing loans	3,082,511	2,976,607
- Family loans	3,109,013	3,369,174
- Consumption loans	97,410	175,694
- Morabaha	846,138	660,608
- Group loans	732,562	1,140,887
- Fast loans	6,537	16,981
- Individual loans	81,877	162,974
	7,956,048	8,502,925
- FATEN employees' loans	173,029	176,924
- NGOs' employees' loans	165,101	264,318
	8,294,178	8,944,167
Provision for loan losses	(639,811)	(275,811)
Loans portfolio – net	**7,654,367**	**8,668,356**
	========	=======

b. The amount of USD 8,294,178 includes the amount of 3,771,068 as loans with accrued installments over 90 days recording without the accrued interest for the period after the 90 days.

c. *By geographical area:*

	Outstanding Balance USD	Provision for loan losses USD	Net realizable value USD
- North Area – West Bank	2,037,431	(166,322)	1,871,109
- South area – West Bank	3,025,833	(242,066)	2,783,767
- Central area – West Bank	338,129	--	338,129
- Gaza	2,892,785	(231,423)	2,661,362
Total	**8,294,178**	**(639,811)**	**7,654,367**
	=======	=======	========

d. The movement in the loans receivable were as follows:

Description	Beginning balance USD	Issued USD	Repaid USD	Loans written-off USD	Ending balance USD
Morabaha	660,694	390,439	(204,995)	--	846,138
Consumption	175,694	131,819	(210,103)	--	97,410
Family loans	3,369,174	1,549,035	(1,809,196)	--	3,109,013
Housing loans	2,,976,607	950,406	(844,502)	--	3,082,511
Group loans	1,140,886	1,137,866	(1,546,190)	--	732,562
Fast loans	16,981	49,068	(59,512)	--	6,537
Individual loans	162,889	25,601	(106,613)	--	81,877
Employees' loans	176,924	122,489	(126,384)	--	173,029
NGO's employees' loans	264,318	103,132	(202,349)	--	165,101
Total	**8,944,167**	**4,459,855**	**(5,109,844)**	**--**	**8,294,178**
	=======	========	========	=====	=======

e. FATEN has an insider loans and loans for related party, and employee loans are Guarantee with end of services, indemnity and provident fund.

f. The movement in the provision for loans losses during the year was as follows:

	2006	2005
	USD	USD
- Balance, beginning of year	275,811	83,442
- Additions during the year	364,000	192,455
- Written-off loans	--	(86)
Balance – ending of year	**639,811**	**275,811**

g. The loan portfolio as at Dec 31, 2006 distributed by maturity as follows:

	2006
	USD
- Up to one year	2,483,050
- From one year to 2 years	2,010,135
- Over two years	3,800,990

h. Collection of written-off:

The management of FATEN wrote-off loans totaling USD 455,754 during the years 2000, 2001 & 2002, amount of USD 311,441 were collected during the period from 2002 till 2006. The balance as at December 31, 2006 was USD 144,313.

5. Other current assets:

	2006	2005
	USD	USD
- Receivable from donors	16,044	487,269
- Prepayments	9,564	14,660
- Accrued bank interests	8,587	393
- Interest receivables	50,890	29,709
Balance – ending of year	**85,085**	**532,031**

6. Fixed assets:

This item consists of:

Description	Buildings	Vehicles	Furniture & equipment	Total
	USD	USD	USD	USD
Balance as at 01/01/2006	319,846	71,991	300,275	692,112
Additions	--	39,211	31,209	70,420
Deductions	--	(17,893)	(1,484)	(19,377)
Balance as at 31/12/2006	**319,846**	**93,309**	**330,000**	**743,155**
Accumulated depreciation				
Balance at 01/01/2006	36,960	71,615	218,645	327,220
Depreciation	6,397	5,096	25,815	37,308
Deductions	--	(17,893)	--	(17,893)
Balance at 31/12/2006	**43,357**	**58,818**	**244,460**	**346,635**
Net book value as at:				
31/12/2006	**276,489**	**34,491**	**85,540**	**396,520**
31/12/2005	**282,886**	**376**	**81,630**	**364,892**

Fixed assets include USD 157,017 of fully depreciated fixed assets that are still operational as at December 31, 2006.

7. Payables and accruals:

This item consists of:

	2006	2005
	USD	USD
- Unearned interest & commission revenue	627,319	605,864
- Customers' savings liability	12,642	32,288
- Accrued audit fees	7,898	7,371
- Others	19,374	24,416
Total	**667,233**	**669,939**

8. Long term loans:

An agreement was signed on October 14, 2004 between *Small Projects Support Program in Palestine* represented by the Islamic Bank for Development and *FATEN* to support the small projects according to the Islamic terms, such as (Morabaha loans and others), which benefits the poor people were affected by bad conditions. The amounts of USD 200,000 from the program and USD 100,000 from FATEN were deposited in special bank account, Arab Bank, A/C# 9550-360500. The amount of USD 200,000 will be settled during the end of the fourth year with zero interest rate beginning from the date of signing the agreement (there were no guarantee for this loan).

9. Provisions for employees' indemnity:

This movement on the provision for employees' indemnity during the year 2006 was as follows:

Description	Beginning balance USD	Additions USD	Payments USD	Total USD
Provident fund	424,358	116,936	(46,131)	495,163
End of service benefit	195,405	47,499	(17,422)	225,482
Total	**619,763**	**164,435**	**(63,553)**	**720,645**

10. Operating and administrative expenses:

a. This item consists of:

	2006 USD	2005 USD
- Salaries and related benefits	643,451	609,599
- Professional fees	18,397	41,697
- Stationery and office supplies	12,796	15,968
- Communication	34,878	33,050
- Transportation and auto operations	57,029	49,233
- Occupancy costs	65,586	55,010
- Equipment rental and maintenance	6,086	7,005
- Depreciation	37,308	44,258
- Other expenses	12,707	26,175
- Bank charges - b	45,748	87,423
- Loss on foreign currency	842	443
Total	**934,828**	**969,861**

c. The amounts of USD 45,748 during 2006 and USD 87,423 during 2005 was paid to the local banks for special services offered by the banks.

11. Accumulated donations, grants and in-kind contribution:

a-This item consists of:

	2006			2005
Description	**Sub-grant # SC/FA 003 Save the Children USD**	**Sub-grant # SC/FA 007 USAID USD**	**Total USD**	**Total USD**
Donations recorded directly to balance sheet	13,154	1,960,097	1,973,251	4,339,262
Grants to subsidize operations	174,268	--	174,268	84,556
Total	***187,422***	***1,960,097***	***2,147,519***	***4,423,818***
Accumulated donations as at 01/01/2006			12,233,519	7,809,701
Accumulated donations as at 31/12/2006			**14,381,038**	**12,233,519**

b- There were no any in-kind of contribution or grants.

12. Fair values of financial instruments:

Financial instruments comprise of financial assets and financial liabilities. Financial assets consist of cash and cash at banks and loans receivable. Financial liabilities consists payables and accruals.

The fair value of financial instruments is not materially different from their carrying values.

13. Construction of main assets and liabilities :

This item consists of:

	2006			
Description	**West Bank**	**Gaza Strip**	**Total**	**2005**
	USD	**USD**	**USD**	**USD**
- Cash in hand and at bank	4,724,677	955,346	5,678,023	2,117,106
- Net loan portfolio	4,993,005	2,661,362	7,654,367	8,668,357
- Other current assets	50,344	34,741	85,085	532,031
- Fixed assets (net)	264,760	131,761	396,521	364,892
- Payable & Accruals	(469,096)	(198,137)	(667,233)	(669,939)
- Long term loan	(200,000)	--	(200,000)	(200,000)

14. Net assets for foreign currencies :

This item consists of:

	2006	**2005**
	USD	**USD**
- Total Assets	13,103,430	10,821,851
- Total Liabilities	972,107	873,931
Net Assets	**12,131,323**	**9,947,920**
	========	=======
- Cash in hand and at bank	5,198,408	1,904,533
- Loan receivables	7,541,728	7,988,206
- Other current assets	363,294	929,112
- Payable & Accruals	51,462	54,168
- Long term loan	200,000	200,000
- Provision for Employee indemnity	720,645	619,763

Foreign currencies: currencies other than the basic currency (Jordanian Dinar).

15. Risk management:

a. Interest rate risk:

FATEN is exposed to interest rate risk on the time deposits that are considered interest-bearing assets (Note 3).

b. Liquidity risk:

FATEN limits its liquidity risk by maintaining adequate cash balances to meet its current obligations and to finance its operating activities.

c. Foreign currency risk:

FATEN maintains its major liabilities and assets in one currency, which is the USD. In addition, its major donation revenues are collected in USD and most of its expenses are paid in USD.

d. Credit risk:

FATEN limits its credit risk by maintaining adequate collateral such as; post-dated checks, promissory notes, notary deeds and transferred salaries.

16. Concentration of risk in geographical area:

FATEN is carrying out all of its activities in Palestine. The political and economical destabilization in the area increases the risk of carrying out these activities and adversely affects the performance.

17. General

Certain comparative figures have been reclassified to comply with this year financial statements presentation.