Palestine for Credit & Development - FATEN
Ramallah – Palestine

Auditors' Report &
Financial Statements
for the year ended December 31, 2005

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 balance sheet of **Palestine for Credit & Development (FATEN)** as at December 31, 2005 and the related statements of income, changes in equity and cash flows for the year then ended. These financial statements are the responsibility of **FATEN's** management. 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 plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly in all material respects, the financial position of **Palestine for Credit & Development (FATEN)** as at December 31, 2005 and the result of its operations and its cash flows for the year then ended, in conformity with International Financial Reporting Standards.

Talal Abu-Ghazaleh & Co.

Jamal Milhem
Certified Public Accountant ***(License No. 100/98)***

Ramallah, March 21, 2006

Palestine for Credit & Development (FATEN)
Ramallah – Palestine
Balance sheet as at December 31, 2005 *Exhibit "A"*

	Note	2005	2004
Assets		**USD**	**USD**
Current assets			
Cash in hand and at banks	(3)	2,118,523	3,491,348
Loans receivable – net	(2b-c, 4a)	8,668,356	2,300,459
Other current assets	(5)	532,031	240,961
Total current assets		**11,318,910**	**6,032,768**
Fixed assets	(2d, 6)		
At cost		692,112	664,851
Accumulated depreciation		(327,220)	(282,962)
Net book value		**364,892**	**381,889**
Total assets		**11,683,802**	**6,414,657**
Liabilities and equity			
Current liabilities			
Payables and accruals	(7)	669,939	99,101
Total current liabilities		**669,939**	**99,101**
Long term loans	(8)	200,000	--
Provisions for employees' indemnity	(9)	619,763	528,081
Total liabilities		**1,489,702**	**627,182**
Equity			
Paid-in capital		4,080	4,080
Accumulated donations	(11)	12,233,519	7,809,701
Accumulated losses		(2,043,499)	(2,026,306)
Total net assets		**10,194,100**	**5,787,475**
Total liabilities and net assets		**11,683,802**	**6,414,657**

"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, 2005

Exhibit "B"

	Note	2005 USD	2004 USD
Revenues			
Interest and fees on loans		1,061,668	430,021
Provision for loan losses	(4)	(192,455)	(9,398)
Net interest income		**869,213**	**420,623**
Other operating revenues			
Collection of loans previously written-off		20,765	46,873
Application fees		14,407	61,148
Penalty fees and others		4,675	34,306
Bank interests		24,534	27,805
Other revenues		19,074	12,846
Total other operating revenues		**83,455**	**182,978**
Total operating revenues		**952,668**	**603,601**
Operating and administrative expenses	(10)	(969,861)	(858,588)
Net operating loss		**(17,193)**	**(254,987)**
Grants to subsidies operations	(11)	84,556	254,987
Net profit after grants		**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, 2005

Exhibit "C"

Description	Paid in capital USD	Accumulated donations USD	Accumulated losses USD	Total USD
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**
Balance as at 01/01/2004	4,080	6,751,008	(1,771,319)	4,983,769
Donations recorded directly to balance sheet	--	803,706	--	803,706
Grants to subsidies operations	--	254,987	--	254,987
Net operating loss for the year	--	--	(254,987)	(254,987)
Balance as at 31/12/2004	**4,080**	**7,809,701**	**(2,026,306)**	**5,787,475**
	======	=======	========	=======

"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, 2005

Exhibit "D"

Operating activities	Note	2005 USD	2004 USD
Net operating loss		(17,193)	(254,987)
Adjustments to reconcile changes in net assets during the year to net cash used for (provided from) activities			
Non cash items			
Depreciation expenses	(6)	44,258	50,340
Gain on sale of fixed assets		--	(3,924)
Provision for loan losses	(4d)	192,455	9,398
Written-off loans	(4d)	(86)	--
Provision for employees' indemnity	(9)	137,541	136,551
Changes in current assets and current liabilities:			
Increase in other current assets		(291,070)	(212,883)
Increase in payable and accruals		570,838	4,102
Employees' indemnity paid	(9)	(45,859)	(81,554)
Net cash flows provided from (used by) operating activities		**590,884**	**(352,957)**
Cash flows from investing activities:			
Net increase in loans receivable		(6,560,266)	(1,122,234)
Proceed from sale of fixed assets		--	7,161
Purchase of fixed assets	(6)	(27,261)	--
Net cash used by investing activities		**(6,587,527)**	**(1,115,073)**
Cash flows from financing activities			
Donations and grants	(11)	4,423,818	1,058,693
Long term loans	(8)	200,000	--
Net cash provided from financing activities		**4,623,818**	**1,058,693**
Decrease in cash and cash equivalent		(1,372,825)	(409,337)
Cash and cash equivalent – beginning of year	(3)	3,491,348	3,900,685
Cash and cash equivalent – ending of year	**(3)**	**2,118,523**	**3,491,348**

"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 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 66 and 57 employees' as at December 31, 2005 and 2004 respectively.

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.

b. Use of Estimates:

The preparation of the financial statements in conformity with International Financial Reporting Standards requires management to make estimates and assumption 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:

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 below:

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

FATEN is 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. 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 amount.

e. 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.

f. Expenses recognition:

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

g. 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.

h. 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	2004
	JD	JD
- USD	0.71	0.71
- NIS	0.15	0.163

i. 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:

	2005 USD	2004 USD
- Cash in hand	1,417	1,380
- Cash at banks- NIS	10,095	6,244
- Cash at banks – JD	213,989	234,957
- Cash at banks - USD	825,589	--
- Deposit at bank – USD - b	610,984	2,837,669
Total	1,662,074	3,080,250
Deposits restricted for employees' indemnity - b	456,449	411,098
Total	**2,118,523**	**3,491,348**

b. Bank deposits at Al-Quds bank in Palestine are short term in nature, with an average interest rate of 2% for deposits in USD.

4. Loans receivables:

a. By type of loans:

	2005 USD	2004 USD
- Housing loans	2,976,607	--
- Family loans	3,369,174	583,970
- Consumption loans	175,694	--
- Morabaha	660,608	--
- Group loans	1,140,887	1,160,737
- Fast loans	16,981	26,300
- Individual loans	162,974	137,506
	8,502,925	1,908,513
- FATEN employees' loans	176,924	127,445
- NGOs' employees' loans	264,318	347,943
	8,944,167	2,383,901
Provision for loan losses	(275,811)	(83,442)
Loans receivable – net	**8,668,356**	**2,300,459**

b. By geographical area:

	Outstanding balance USD	Provision for loan losses USD	Net realizable value USD
- North Area – West Bank	2,170,137	(83,810)	2,086,327
- South area – West Bank	2,022,460	(95,331)	1,927,129
- Central area – West Bank	1,710,012	--	1,710,012
- Gaza	3,041,558	(96,670)	2,944,888
	8,944,167	**(275,811)**	**8,668,356**

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

Description	Beginning balance USD	Issued USD	Repair USD	Loans written-off USD	Ending balance USD
Morabaha	--	746,909	(86,215)	--	660,694
Consumption	--	258,059	(82,365)	--	175,694
Family loans	583,970	3,832,704	(1,047,500)	--	3,369,174
Housing loans	--	3,191,621	(215,014)	--	2,976,607
Group loans	1,160,737	3,092,304	(3,112,155)	--	1,140,886
Fast loans	26,300	246,800	(256,119)	--	16,981
Individual loans	137,506	228,360	(202,891)	(86)	162,889
Employees' loans	127,445	181,298	(131,819)	--	176,924
NGO's employees' loans	347,943	206,148	(289,773)	--	264,318
	2,383,901	**11,984,203**	**(5,423,851)**	**(86)**	**8,944,167**
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d. The movement in the provision for loans losses during the year was as follows:

	2005 USD	2004 USD
- Balance, beginning of year	83,442	74,044
- Additions during the year	192,455	9,398
- Written-off loans	(86)	--
Balance – ending of year	**275,811**	**83,442**
	======	======

e. Collection of written-off:

The management of FATEN wrote-off loans totaling USD 455,754 during the years 2000, 2001 & 2002, amount of USD 302,778 were collected during the period from 2002 till 2005. The balance as at December 31, 2005 was USD 152,975.

5. Other current assets:

	2005 USD	2004 USD
- Receivable from donors	487,269	224,270
- Prepayments	30,102	13,125
- Others	14,660	3,566
Balance – ending of year	**532,031**	**240,961**
	======	======

6. Fixed assets:

This item consists of:

Description	Buildings	Vehicles	Furniture & equipment	Total
	USD	USD	USD	USD
Balance as at 01/01/2005	319,846	71,991	273,014	664,851
Additions	--	--	27,261	27,261
Deductions	--	--	--	--
Balance as at 31/12/2005	**319,846**	**71,991**	**300,275**	**692,112**
Accumulated depreciation				
Balance at 01/01/2005	30,563	62,210	190,189	282,962
Depreciation	6,397	9,405	28,456	44,258
Balance at 31/12/2005	**36,960**	**71,615**	**218,645**	**327,220**
Net book value as at:				
31/12/2005	**282,886**	**376**	**81,630**	**364,892**
31/12/2004	**289,283**	**9,781**	**82,825**	**381,889**

Fixed assets include USD 67,996 of fully depreciated fixed assets that are still operational as at December 31, 2005.

7. Payables and accruals:

This item consists of:

	2005	2004
	USD	USD
- Unearned interest revenue	605,864	35,641
- Customers' savings liability	32,288	39,403
- Due to suppliers	7,371	10,530
- Others	24,416	13,527
Total	**669,939**	**99,101**

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 beginning from the date of signing the agreement.

9. Provisions for employees' indemnity:

This movement on the provision for employees' indemnity during the year 2005 was as follows:

Description	Beginning balance USD	Additions USD	Payments USD	Total USD
Provident fund	361,712	93,366	30,720	424,358
End of service benefit	166,369	44,175	15,139	195,405
Total	**528,081**	**137,l541**	**45,859**	**619,763**
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10. Operating and administrative expenses:

a. This item consists of:

	2005 USD	2004 USD
- Salaries and related benefits	609,599	624,201
- Professional fees	41,697	17,280
- Stationery and office supplies	15,968	11,110
- Communication	33,050	40,242
- Transportation	49,233	36,893
- Occupancy costs	56,208	47,962
- Equipment rental and maintenance	7,005	20,799
- Depreciation	44,258	50,340
- Other expenses	25,420	9,761
- Bank charges - b	87,423	--
Total	**969,861**	**858,588**
	======	========

b. The amount of 87,423 was paid to the local banks for special services offered by the banks.

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

This item consists of:

	2005			2004
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	16,983	4,322,279	4,339,262	803,706
Grants to subsidize operations	84,556	--	84,556	254,987
Total	***101,539***	***4,322,279***	***4,423,818***	***1,058,693***
Accumulated donations as at 01/01/2005			7,809,701	6,751,008
Accumulated donations as at 31/12/2005			**12,233,519**	**7,809,701**
			========	========

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 consist payables and accruals.

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

13. 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.

14. Concentration of risk in geographical area:

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