

REEF FINANCE COMPANY (NOT FOR PROFIT)

FINANCIAL STATEMENTS

FOR THE YEAR ENDED DECEMBER 31, 2012

AND INDEPENDENT AUDITOR'S REPORT

REEF FINANCE COMPANY (NOT FOR PROFIT)

Financial statements for the year ended December 31, 2012

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Independent Auditor's Report

**To the Board of Directors
Reef Finance Company**

Report on the financial statements

We have audited the accompanying financial statements of Reef Finance Company – not for profit (hereinafter “Reef”), which comprise the statement of financial position as of December 31, 2012, statement of income and other comprehensive income, statement of changes in equity and statement of cash flows for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management's responsibility for the financial statements

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

Opinion on the financial statements

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of Reef as of December 31, 2012, and the results of its activities and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers Palestine Limited
Ramallah: May 26, 2013

PricewaterhouseCoopers Palestine Limited, P.O.Box 1317, Masrouji Building 201, El-Bireh (Ramallah), Palestine
T: +972 (0) 2 242 0230, F: +972 (0) 2 242 0231 Note: From Arab Countries Dial 970 instead of 972,
www.pwc.com/middle-east

REEF FINANCE COMPANY (NOT FOR PROFIT)

Financial statements for the year ended December 31, 2012

STATEMENT OF FINANCIAL POSITION

(All amounts in US Dollar)

| | <u>Note</u> | <u>2012</u> | <u>2011 Restated Note (22)</u> |
|---|-------------|------------------|--|
| Assets | | | |
| Non-current assets | | | |
| Property and equipment | (5) | 51,898 | 66,498 |
| Current assets | | | |
| Loans receivable | (6) | 6,517,200 | 4,683,138 |
| Deposit with Palestinian Monetary Authority | (7) | 30,439 | 30,439 |
| Contributions receivable | (8) | 366,857 | - |
| Other current assets | (9) | 78,005 | 72,254 |
| Cash and cash equivalents | (10) | 1,278,291 | 3,200,245 |
| Total current assets | | 8,270,792 | 7,986,076 |
| Total assets | | 8,322,690 | 8,052,574 |
| Equity, subordinate loan and liabilities | | | |
| Equity and subordinate loan | | | |
| Share capital | (11) | 200,000 | 195,500 |
| Retained earnings | | 4,036,718 | 2,993,910 |
| Temporarily restricted contributions | (8) | 1,059,460 | 1,340,782 |
| Total equity | | 5,296,178 | 4,530,192 |
| Subordinate loan | (12) | 1,500,000 | 1,500,000 |
| Total equity and subordinate loan | | 6,796,178 | 6,030,192 |
| Liabilities | | | |
| Non-current liabilities | | | |
| Long term loans | (13) | 667,008 | 1,333,257 |
| Provision for employees' indemnity | (14) | 243,648 | 204,400 |
| Total non-current liabilities | | 910,656 | 1,537,657 |
| Current liabilities | | | |
| Long term loan-matures during next year | (13) | 552,444 | 433,096 |
| Cash margins | (15) | 13,815 | 19,919 |
| Payables and accruals | (16) | 49,597 | 31,710 |
| Total current liabilities | | 615,856 | 484,725 |
| Total liabilities | | 1,526,512 | 2,022,382 |
| Total Equity, subordinate loan and liabilities | | 8,322,690 | 8,052,574 |

- The notes on pages 7 to 21 are an integral part of these financial statements.

- The financial statements on page 3 to 21 were authorized for issue by the Board of Directors on May 15, 2013 and were signed on its behalf.

Mr. Khalil Sheeha
Chairman of the Board

Mr. Mohammad Abo Dalo
General Manager

REEF FINANCE COMPANY (NOT FOR PROFIT)

Financial statements for the year ended December 31, 2012

STATEMENT OF INCOME AND OTHER COMPREHENSIVE INCOME

(All amounts in US Dollar)

| | <u>Note</u> | <u>2012</u> | <u>2011 Restated Note (22)</u> |
|--|-------------|-------------------------|--|
| <u>Revenues</u> | | | |
| Temporarily restricted contributions released from restriction | (8) | 1,165,767 | 1,981,389 |
| Financing income | (17) | 771,060 | 506,127 |
| Commission | (17) | 2,424 | 50,386 |
| Other revenues | | 29,015 | 15,051 |
| Total Revenues | | <u>1,968,266</u> | <u>2,552,953</u> |
| <u>Expenses</u> | | | |
| General & Administrative expenses | (18) | 638,101 | 464,817 |
| General & Administrative expenses covered by donors | (18) | 203,047 | 367,491 |
| Finance expenses | (19) | 66,872 | 36,231 |
| Allowance for doubtful loans | (6) | (7,735) | 197,380 |
| Depreciation expense | (5) | 25,173 | 23,497 |
| Total Expenses | | <u>925,458</u> | <u>1,089,416</u> |
| Profit for the year before other comprehensive income | | <u>1,042,808</u> | <u>1,463,537</u> |
| Other comprehensive income | | <u>-</u> | <u>-</u> |
| Profit for the year after other comprehensive income | | <u>1,042,808</u> | <u>1,463,537</u> |

- The notes on pages 7 to 21 are an integral part of these financial statements.

REEF FINANCE COMPANY (NOT FOR PROFIT)-REEF
 Financial statements for the year ended December 31, 2012

STATEMENT OF CHANGES IN EQUITY

(All amounts in US Dollar)

| | <u>Note</u> | <u>Share capital</u> | <u>Retained earnings</u> | <u>Total</u> |
|--|-------------|----------------------|--------------------------|------------------|
| Balance as of January 1,2011 | | 185,500 | 1,240,295 | 1,425,795 |
| Prior period adjustments | (22) | - | 290,078 | 290,078 |
| Adjusted balance as of January 1, 2011 | | 185,500 | 1,530,373 | 1,715,873 |
| Issue of share capital | | 10,000 | - | 10,000 |
| Profit for the year after other comprehensive income | | - | 1,463,537 | 1,463,537 |
| Balance as of December 31,2011 | | 195,500 | 2,993,910 | 3,189,410 |
| Issue of share capital | (11) | 4,500 | - | 4,500 |
| Profit for the year after other comprehensive income | | - | 1,042,808 | 1,042,808 |
| Balance as of December 31,2012 | | 200,000 | 4,036,718 | 4,236,718 |

- The notes on pages 7 to 21 are an integral part of these financial statements.

STATEMENT OF CASH FLOWS

(All amounts in US Dollar)

| | <u>2012</u> | <u>2011 Restated Note (22)</u> |
|--|--------------------------------|--|
| Cash flows from operating activities | | |
| Profit for the year | 1,042,808 | 1,463,537 |
| Adjustments for: | | |
| Provision for employees' indemnity | 85,511 | 76,601 |
| Depreciation | 25,173 | 23,497 |
| Provision for doubtful loans | (7,735) | 197,380 |
| Cash flows before changes in working capital | <u>1,145,757</u> | <u>1,761,015</u> |
| Changes in working capital: | | |
| Contributions receivable | (366,857) | 2,542 |
| Other current assets | (5,751) | (37,386) |
| Cash margin | (6,104) | (1,642) |
| Payables and accruals | 17,887 | (2,311) |
| Cash used in operating activities | <u>(360,825)</u> | <u>(38,797)</u> |
| Loans receivable | (1,826,327) | (1,554,627) |
| Payments of employees' indemnity | (46,263) | (18,151) |
| Net cash (used in) provided by operating activities | <u>(1,087,658)</u> | <u>149,440</u> |
| Cash flows used in investing activities | | |
| Purchase of property and equipment | (10,573) | (32,139) |
| Net cash flows used in investing activities | <u>(10,573)</u> | <u>(32,139)</u> |
| Cash flows from financing activities | | |
| Proceeds from share capital settlement | 4,500 | 10,000 |
| Proceeds from borrowings - Loans | - | 1,308,395 |
| Repayments of borrowings - Loans | (546,901) | (275,101) |
| Temporarily restricted contributions | (281,322) | (510,646) |
| Net cash flows (used in) provided by financing activities | <u>(823,723)</u> | <u>532,648</u> |
| Change in cash and cash equivalents | <u>(1,921,954)</u> | <u>649,949</u> |
| Cash and cash equivalents ,beginning of the year | <u>3,200,245</u> | <u>2,550,296</u> |
| Cash and cash equivalents, end of year | <u><u>1,278,291</u></u> | <u><u>3,200,245</u></u> |

- The notes on pages 7 to 21 are an integral part of these financial statements.

REEF FINANCE COMPANY (NOT FOR PROFIT)

Financial statements for the year ended December 31, 2012

NOTES TO THE FINANCIAL STATEMENTS

(All amounts are in US Dollar)

NOTE (1) GENERAL

Reef Finance Company ("Reef" or "the Company") is a Palestinian private not for profit company registered on July 2, 2007 in Gaza under registration number of (563143734) with an authorized capital of USD 200,000 as of December 31, 2012 (2011 USD 200,000).

Reef provides diversified financial services directed towards micro and small businesses, especially in rural areas. Most of Reef loans represent in-kind loans, where Reef disburses the funds directly to the suppliers.

The Company's parent, The Palestinian Agriculture Relief Committees, (hereinafter "PARC"), signed an agreement on August 30, 2007 with the Netherlands Representative Office to the Palestinian Authority in the amount of USD 2,747,385 to establish Reef Finance Company.

NOTE (2) BASIS OF PREPARATION

The principal accounting policies applied in the preparation of these financial statements are set below. These policies have been consistently applied to all years presented, unless otherwise stated.

Basis of preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards. The financial statements have been prepared under the historical cost convention.

Critical accounting estimates and assumptions

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Company's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in note 4.

Changes in accounting policies and disclosures

(a) New and amended standards adopted by the entity

- There are no IFRSs or IFRIC interpretations that are effective for the first time for the financial year beginning on or after 1 January 2012 that would have had a material impact on Reef.

(b) New standards, amendments and interpretations issued but not effective and applicable for the financial year beginning 1 January 2012 and not early adopted

- IAS 19, 'Employee benefits' was amended in June 2011.
- IFRS 9, 'Financial instruments', addresses the classification, measurement and recognition of financial assets and financial liabilities.

(c) Restatement of financial statements

Starting January 1, 2012, Reef changed its accounting policy regarding the recognition of financing income. The financial statements, including prior year's comparative figures, are presented as if the new accounting policy has been applied from January 1, 2011. Therefore, comparative figures for the year ended December 31, 2011 are restated in order to reflect the new accounting policy. The nature of the change and the effect of the restatement are depicted in note 22.

Foreign currency translation

(a) Functional and presentation currency

Items included in the financial statements are measured using the currency of the primary economic environment in which Reef operates which is the US Dollar (USD). The financial statements are presented in USD, which is Reef's presentation currency.

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuation where items are re-measured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the statement of income and other comprehensive income.

REEF FINANCE COMPANY (NOT FOR PROFIT)

Financial statements for the year ended December 31, 2012

NOTES TO THE FINANCIAL STATEMENTS

(All amounts are in US Dollar)

Property and equipment

Property and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to Reef and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are charged to the statement of income and other comprehensive income during the financial period in which they are incurred.

Depreciation on other assets is calculated using the straight-line method to allocate their cost amounts to their residual values over their estimated useful lives, as follows:

| | <u>Useful life (Years)</u> |
|-------------------------------|----------------------------|
| Office furniture | 7 |
| Office equipment | 5 |
| Lease hold improvements | 4 |
| Computer software | 4 |
| Control and protection system | 4 |

The asset's residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within the statement of income and other comprehensive income.

Cash and cash equivalents

Cash and cash equivalents include cash at bank, cash on hand and short-term deposits with an original maturity of three months or less.

Net assets

Net assets of Reef and changes therein are classified and reported as follows:

- Unrestricted net assets - Net assets whose use by Reef is not subject to donor-imposed restrictions and whose restrictions are met in the same reporting period.
- Temporarily restricted net assets - Net assets whose use by Reef is limited by donor-imposed stipulations that limits the use of the donation. When donor restriction expires, temporarily restricted contributions are reclassified to unrestricted net assets and reported in the statement of income and other comprehensive income as contributions released from restrictions.

Revenue recognition

a) Donations revenue

- Unrestricted contributions and/or donations are recognized in the statement of income and other comprehensive income when received.
- Restricted contributions and/or donations are recognized when received and/or when the related project expenditures exceeded the received amount. The excess of the project expenditures over the received amount is recognized as contribution receivables under financing income.

b) Financing income

- Financing income from loans is recognized using the effective interest method over the financing period.
- Murabaha profits collected from borrowers on the date of transaction are recognized immediately in the statement of income and other comprehensive income.

c) Commission revenues

Commissions are recognized as revenues when the related service is rendered.

Expense recognition

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

REEF FINANCE COMPANY (NOT FOR PROFIT)

Financial statements for the year ended December 31, 2012

NOTES TO THE FINANCIAL STATEMENTS

(All amounts are in US Dollar)

Loans receivable

Loans are stated at the amount of outstanding principal reduced by an allowance for loan losses. In determining the value of the allowance, variables taken into consideration including experience gained from previous losses, the present economic situation and its effects on loan holders, and the limit of commitment of individuals to the terms of the loan. The allowance is determined based on the management estimations.

Reef established general and specific allowances for doubtful loans based on past collection experience and other factors that may affect collectability.

Loans are written off in case the procedures taken for collecting the loans are ineffective. Any subsequent collections in respect of such loans that have been written off are included within the statement of income and other comprehensive income.

Long term loans

Long term loans are recognized initially at fair value, net of transaction costs incurred. Long term loans are subsequently carried at amortized cost.

Payables and accruals

Liabilities are recognized for amounts to be paid in the future for goods or services received whether billed by the supplier or not.

Provisions for employees' indemnity and provident fund

Reef provides employees with end of services benefits by accruing 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. Reef also provides employees with a provident fund; contributions by the employees and Reef are set at 5% and 10%, respectively, based on the employees' basic monthly salaries.

NOTE (3) RISK MANAGEMENT

Reef activities expose it to a variety of financial risks: market risk (including currency risk), credit risk and liquidity risk. Reef's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on Reef's financial performance.

Risk management is carried out by the finance department under policies approved by the board of directors. The Finance department identifies and evaluates financial risks in close co-operation with Reef's operating units. The board provides written principles for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest rate risk and credit risk.

Market risk:

A. Currency risk

Currency risk is defined as the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. However, Reef mitigates this risk by maintaining all its financial instruments in USD and signing all its agreements (loans or others) in USD, while any other liabilities or assets in other currencies are justified and have a unique condition like grants or loans. Reef keeps the minimum balance of NIS for petty cash and daily expenses.

The main currencies that Reef uses are the United States Dollars (USD), the New Israeli Shekel (NIS) and Jordanian Dinar (JD) as well as the (Euro). Fluctuations in the exchange rates in the year resulted in a loss of USD 2,944 (2011 gain of USD 3,372).

B. Cash flow and fair value interest rate risk

Cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Fair value interest rate risk is the risk that the value of a financial instrument will fluctuate because of changes in market interest rates. Reef takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on both its fair value and cash flow risks. Interest margins may increase as a result of such changes but may reduce losses in the event that unexpected movements arise. The Board sets limits on the level of mismatch of interest rate re-pricing and value at risk that may be undertaken, which is monitored by the credit committee.

REEF FINANCE COMPANY (NOT FOR PROFIT)

Financial statements for the year ended December 31, 2012

NOTES TO THE FINANCIAL STATEMENTS

(All amounts are in US Dollar)

The following table demonstrates the sensitivity to a reasonable possible change in interest rates, with all other variables held constant, of Reef's statement of income and other comprehensive income:

| <u>Currency (2012)</u> | <u>Increase in interest rate</u> | <u>Sensitivity of net interest income</u> |
|------------------------|--------------------------------------|---|
| | % | USD |
| USD | 0.25 | 16,629 |
| USD | 0.5 | 32,586 |
| <u>Currency (2012)</u> | <u>Decrease in interest rate</u> | <u>Sensitivity of net interest income</u> |
| | % | USD |
| USD | 0.25 | (16,629) |
| USD | 0.5 | (32,586) |

| <u>Currency (2011)</u> | <u>Increase in interest rate</u> | <u>Sensitivity of net interest income</u> |
|------------------------|--------------------------------------|---|
| | % | USD |
| USD | 0.25 | 11,708 |
| USD | 0.5 | 23,416 |

| <u>Currency (2011)</u> | <u>Decrease in interest rate</u> | <u>Sensitivity of net interest income</u> |
|------------------------|--------------------------------------|---|
| | % | USD |
| USD | 0.25 | (11,708) |
| USD | 0.5 | (23,416) |

Credit risk

Credit risk is defined as the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. The risk is divided into the following sections:

| <u>Item</u> | <u>Carrying amount 2012</u> | <u>Carrying amount 2011</u> |
|---|---------------------------------|---------------------------------|
| Cash and cash equivalents | 1,278,291 | 3,200,245 |
| Contributions receivable | 366,857 | - |
| Loans receivable | 5,164,788 | 3,919,389 |
| Deposit with Palestinian Monetary Authority | 30,439 | 30,439 |

Cash and cash equivalents are placed in local banks operating in Palestine. These financial institutions do not have credit ratings.

Information on the credit quality of loans is set out in notes 4 and 6 below.

REEF FINANCE COMPANY (NOT FOR PROFIT)

Financial statements for the year ended December 31, 2012

NOTES TO THE FINANCIAL STATEMENTS

(All amounts are in US Dollar)

Liquidity risk:

The risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities. The schedule below presents expected cash outflow resulting from financial liabilities broken down by time brackets:

| Items | Interest rate % | Carrying amounts | Expected timing of cash outflow/inflows (Months) | | | |
|------------------------------------|-----------------|------------------|--|----------------|----------------|---------------|
| | | | 0-6 | 7-12 | 13-24 | More than 24 |
| Outflows: | | | | | | |
| Payables and accruals | | 49,597 | 49,597 | - | - | - |
| Long-term loans as follows: | | | | | | |
| Etimos Loan | 2 | 52,792 | - | - | 52,792 | - |
| DEEP 2 | 2 | 199,998 | 70,666 | 70,666 | 58,666 | - |
| DEEP-Alqard Al-Hassan | free | 444,440 | 83,335 | 83,335 | 277,770 | - |
| DEEP_Al-Quds | free | 500,000 | 111,110 | 111,110 | 222,220 | 55,560 |
| DEEP-Mosharakah | free | 22,222 | 11,111 | 11,111 | - | - |
| Total long term loans | | 1,219,452 | 276,222 | 276,222 | 611,448 | 55,560 |
| Grand total | | 1,269,049 | 325,819 | 276,222 | 611,448 | 55,560 |
| Inflows: | | | | | | |
| Cash and cash equivalents | | 1,278,291 | 375,406 | 276,216 | 571,109 | 55,560 |

REEF FINANCE COMPANY (NOT FOR PROFIT)Financial statements for the year ended December 31, 2012

NOTES TO THE FINANCIAL STATEMENTS

(All amounts are in US Dollar)

NOTE (4) CRITICAL ESTIMATES AND JUDGMENTS

The Company makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are addressed below.

A. Interest income

Reef uses the flat rate to calculate interest income on the loan portfolio. The interest rate varies based on management estimate and judgment about the borrower risk and credit rating. This process is handled by the Company's credit committee. Because of the large number of loans and short repayment periods, Reef management considers that recognition of income approximates the use of the effective interest rate method on an individual loan basis.

Reef collects the interest either in advance or as a part of the repayments. Reef recognizes interest collected in advance at the date of each transaction in the statement of income and other comprehensive income as detailed in note (22).

B. Provision against loans receivable

Reef estimates the requirements for provisions against overdue installments as below:

Specific allowance: Specific allowance is calculated as percentage of the loan outstanding balance, based on the amounts past due in each aging category, the following rates are used to calculate the specific provision during 2012:

| Loan status | Allowance (Percent %) |
|----------------------------|----------------------------------|
| 15-30 days overdue | 5 |
| 31-60 days overdue | 15 |
| 61-90 days overdue | 25 |
| 91-180 days overdue | 50 |
| More than 180 days overdue | 100 |

General allowance: General allowance is calculated as percentage of 0.5% of the total loan portfolio at the year end.

REEF FINANCE COMPANY (NOT FOR PROFIT)

Financial statements for the year ended December 31, 2012

NOTES TO THE FINANCIAL STATEMENTS

(All amounts are in US Dollar)

NOTE (5) PROPERTY AND EQUIPMENT

Details 2011:

| | <u>Office furniture</u> | <u>Office equipment</u> | <u>Lease hold improvements</u> | <u>Computer Software</u> | <u>Control and protection system</u> | <u>Total</u> |
|---|-------------------------|-------------------------|--------------------------------|--------------------------|--------------------------------------|----------------|
| Cost | | | | | | |
| Balance January 1, 2011 | 27,980 | 58,261 | 4,077 | 17,517 | - | 107,835 |
| Additions | 5,372 | 13,425 | 5,252 | 3,600 | 4,490 | 32,139 |
| Disposals | - | - | - | - | - | - |
| Balance December 31, 2011 | 33,352 | 71,686 | 9,329 | 21,117 | 4,490 | 139,974 |
| Accumulated depreciation | | | | | | |
| Balance January 1, 2011 | 8,211 | 28,277 | 1,256 | 12,235 | - | 49,979 |
| Additions | 4,446 | 13,133 | 1,628 | 3,781 | 509 | 23,497 |
| Disposals | - | - | - | - | - | - |
| Balance December 31, 2011 | 12,657 | 41,410 | 2,884 | 16,016 | 509 | 73,476 |
| Net book value December 31, 2011 | 20,695 | 30,276 | 6,445 | 5,101 | 3,981 | 66,498 |

Details 2012:

| | <u>Office furniture</u> | <u>Office equipment</u> | <u>Lease hold improvements</u> | <u>Computer Software</u> | <u>Control and protection system</u> | <u>Total</u> |
|---|-------------------------|-------------------------|--------------------------------|--------------------------|--------------------------------------|----------------|
| Cost | | | | | | |
| Balance January 1, 2012 | 33,352 | 71,686 | 9,329 | 21,117 | 4,490 | 139,974 |
| Additions | 2,924 | 4,438 | 730 | 2,481 | - | 10,573 |
| Disposals | - | - | - | - | - | - |
| Balance December 31, 2012 | 36,276 | 76,124 | 10,059 | 23,598 | 4,490 | 150,547 |
| Accumulated depreciation | | | | | | |
| Balance January 1, 2012 | 12,657 | 41,410 | 2,884 | 16,016 | 509 | 73,476 |
| Additions | 5,192 | 14,485 | 2,517 | 2,078 | 901 | 25,173 |
| Disposals | - | - | - | - | - | - |
| Balance December 31, 2012 | 17,849 | 55,895 | 5,401 | 18,094 | 1,410 | 98,649 |
| Net book value December 31, 2012 | 18,427 | 20,229 | 4,658 | 5,504 | 3,080 | 51,898 |

REEF FINANCE COMPANY (NOT FOR PROFIT)

Financial statements for the year ended December 31, 2012

NOTES TO THE FINANCIAL STATEMENTS

(All amounts are in US Dollar)

NOTE (6) LOANS RECEIVABLE

Following are the loans by category:

| | <u>2012</u> | <u>2011</u> |
|------------------------------------|------------------|------------------|
| Individual loans | 6,717,488 | 4,849,193 |
| Group loans | 174,995 | 216,963 |
| Total portfolio | 6,892,483 | 5,066,156 |
| Less: allowance for doubtful loans | 375,283 | 383,018 |
| | 6,517,200 | 4,683,138 |

Loans are classified as follows:

| | <u>2012</u> | <u>2011</u> |
|--------------------------|------------------|------------------|
| Matures during next year | 1,022,287 | 751,408 |
| Matures over one year | 5,870,196 | 4,314,748 |
| | 6,892,483 | 5,066,156 |

Past due and impaired assets

The following provides details of past due assets that are impaired and the related provisions as of December 31, 2012:

| <u>Item</u> | <u>Carrying amount</u> | <u>Aging (Days)</u> | | | | |
|------------------------------|------------------------|---------------------|--------------|--------------|---------------|----------------------|
| | | <u>15-30</u> | <u>31-60</u> | <u>61-90</u> | <u>91-180</u> | <u>More than 180</u> |
| Loans receivable | 1,727,695 | 1,052,040 | 246,114 | 99,322 | 138,570 | 191,649 |
| Allowance for doubtful loans | 375,283 | 52,601 | 36,917 | 24,831 | 69,285 | 191,649 |

In order to face this risk, Reef follows up with the borrowers in order to collect all amounts due. In addition Reef calls the guarantors to collect the overdue loans. If these procedures do not work, Reef files claims in the court against the loan holder.

Following is the movement on the allowance for doubtful loans:

| | <u>2012</u> | <u>2011</u> |
|---------------------------------------|----------------|----------------|
| Beginning balance | 383,018 | 185,638 |
| (Recovered) additions during the year | (7,735) | 197,380 |
| Ending balance | 375,283 | 383,018 |

Following is the distribution of loans for the year 2012 by geographic area:

| | <u>Outstanding Balance</u> | <u>Allowance for doubtful loans</u> | <u>Net realized value</u> |
|-------------------------------------|----------------------------|-------------------------------------|---------------------------|
| Ramallah and North of the West Bank | 961,227 | (79,930) | 881,297 |
| South of the West Bank | 2,030,999 | (105,042) | 1,925,957 |
| Nablus | 1,967,984 | (160,927) | 1,807,057 |
| Gaza | 1,932,273 | (29,384) | 1,902,889 |
| | 6,892,483 | (375,283) | 6,517,200 |

Following is the distribution of loans for the year 2011 by geographic area:

| | <u>Outstanding Balance</u> | <u>Allowance for doubtful loans</u> | <u>Net realized value</u> |
|-------------------------------------|----------------------------|-------------------------------------|---------------------------|
| Ramallah and North of the West Bank | 810,558 | (142,339) | 668,219 |
| South of the West Bank | 1,424,514 | (95,594) | 1,328,920 |
| Nablus | 1,966,211 | (136,842) | 1,829,369 |
| Gaza | 864,873 | (8,243) | 856,630 |
| | 5,066,156 | (383,018) | 4,683,138 |

REEF FINANCE COMPANY (NOT FOR PROFIT)Financial statements for the year ended December 31, 2012

NOTES TO THE FINANCIAL STATEMENTS

(All amounts are in US Dollar)

NOTE (6) LOANS RECEIVABLE (CONTINUED)

Following is the movement on the loans balance during 2012:

| | <u>Beginning balance</u> | <u>Issued loans</u> | <u>Repayments</u> | <u>Ending balance</u> |
|------------------|--------------------------|-------------------------|---------------------------|-------------------------|
| Individual loans | 4,849,193 | 5,122,795 | (3,254,500) | 6,717,488 |
| Group loans | 216,963 | 80,000 | (121,968) | 174,995 |
| Total | <u>5,066,156</u> | <u>5,202,795</u> | <u>(3,376,468)</u> | <u>6,892,483</u> |

Following is the movement on the loans balance during 2011:

| | <u>Beginning balance</u> | <u>Issued loans</u> | <u>Repayments</u> | <u>Ending balance</u> |
|------------------|--------------------------|-------------------------|---------------------------|-------------------------|
| Individual loans | 3,241,959 | 4,477,650 | (2,870,416) | 4,849,193 |
| Group loans | 269,570 | 95,000 | (147,607) | 216,963 |
| Total | <u>3,511,529</u> | <u>4,572,650</u> | <u>(3,018,023)</u> | <u>5,066,156</u> |

REEF FINANCE COMPANY (NOT FOR PROFIT)

Financial statements for the year ended December 31, 2012

NOTES TO THE FINANCIAL STATEMENTS

(All amounts are in US Dollar)

NOTE (6) LOANS RECEIVABLE (CONTINUED)

Following are the loans by sector/ category:

| Loan sector/category | 1-2 months | | 3-4 months | | 5-8 months | | 9-12 months | | 13-18 months | | 18-24 months | | 25-36 months | | 37- over | | Total |
|---------------------------|----------------|-----------------------|---------------|-----------------------|----------------|-----------------------|----------------|-----------------------|------------------|-----------------------|------------------|-----------------------|------------------|-----------------------|------------------|-----------------------|------------------|
| | Amount | Average interest rate | Amount | Average interest rate | Amount | Average interest rate | Amount | Average interest rate | Amount | Average interest rate | Amount | Average interest rate | Amount | Average interest rate | Amount | Average interest rate | |
| Agriculture | 198,199 | 8.52 | 30,203 | 9.63 | 169,761 | 9.40 | 405,709 | 8.00 | 940,378 | 6.84 | 821,737 | 7.86 | 1,518,684 | 8.11 | 108,617 | 4.00 | 4,193,288 |
| Structures and real state | - | - | 695 | 8.56 | 2,303 | 8.75 | 7,273 | 9.80 | 17,314 | 8.94 | 126,977 | 8.55 | 374,124 | 7.83 | 886,066 | 9.00 | 1,414,752 |
| Trading | 12,044 | 10.20 | 3,324 | 11.43 | 37,019 | 10.24 | 77,704 | 9.90 | 101,503 | 11.15 | 160,104 | 10.76 | 632,070 | 10.33 | 8,699 | 9.00 | 1,032,467 |
| Industry and mining | - | - | 900 | 7.00 | - | - | 18,599 | 9.33 | - | - | 22,640 | 9.38 | 7,200 | 12 | - | - | 49,339 |
| Consuming and personal | 2,686 | 3.27 | 5,187 | 2.78 | 5,771 | 8.49 | 42,516 | 2.87 | 90,428 | 3.71 | 10,067 | 2.50 | 5,605 | 2.5 | 1,300 | 3.00 | 163,560 |
| Public services | - | - | 364 | 10.50 | 2,031 | 5.85 | - | - | 2,701 | 11.00 | 6,627 | 9.01 | 27,354 | 7.54 | - | - | 39,077 |
| | 212,929 | | 40,673 | | 216,885 | | 551,801 | | 1,152,324 | | 1,148,152 | | 2,565,037 | | 1,004,682 | | 6,892,483 |

NOTE (7) DEPOSIT WITH PALESTINIAN MONETARY AUTHORITY

During the year 2009, Reef has entered into a Memorandum of Understanding (MoU) with Palestine Monetary Authority (PMA). As per this MoU, Reef has deposited an amount of US Dollar 30,000 with the PMA. Pursuant to this MoU, Reef will have access to benefits from services provided by PMA. On the other hand, Reef is obligated to comply with the PMA rules and regulations in respect of reporting and lending procedures. The amount deposited is accruing interest income subject to the international interest rates at 0.3% per annum.

REEF FINANCE COMPANY (NOT FOR PROFIT)

Financial statements for the year ended December 31, 2012

NOTES TO THE FINANCIAL STATEMENTS

(All amounts are in US Dollar)

NOTE (8) CONTRIBUTIONS RECEIVABLE AND TEMPORARILY RESTRICTED CONTRIBUTIONS

Details 2012:

| | Balance beginning of the year | | | Released from restriction | Currency variance | Balance ending of the year | |
|--|--------------------------------------|-------------------------|----------------|---------------------------|-------------------|--------------------------------------|-------------------------|
| | Temporarily restricted contributions | Contribution receivable | Cash received | | | Temporarily restricted contributions | Contribution receivable |
| Palestinian Agricultural Relief Committee (PARC) – Donated equity* | 800,000 | - | - | - | - | 800,000 | - |
| European Commission (EC) | 37,084 | - | 290,341 | (696,807) | 2,525 | - | (366,857) |
| Institution strengthening Reef Finance Co.- Netherland | 347,498 | - | 224,722 | (412,760) | - | 159,460 | - |
| Declining Musharakeh - UNDP | 100,000 | - | - | - | - | 100,000 | - |
| UNDP - Deep | 56,200 | - | - | (56,200) | - | - | - |
| | 1,340,782 | - | 515,063 | (1,165,767) | 2,525 | 1,059,460 | (366,857) |

*During year 2009, Reef received a total amount of US Dollar 800,000. This amount has been donated by the Government of the Netherlands through PARC - Parent.

As per the donor's stipulations, the amount has been disbursed as loans. Further, the donor has stipulated that this amount should be classified as donated equity on the statement of financial position. However, as of December 31, 2011, the amount was still not registered with the company's controller registrar; accordingly the amount is classified as a temporarily restricted contribution.

Details 2011:

| | Balance beginning of the year | | | Released from restriction | Currency variance | Balance ending of the year | |
|---|--------------------------------------|-------------------------|------------------|---------------------------|-------------------|--------------------------------------|-------------------------|
| | Temporarily restricted contributions | Contribution receivable | Cash received | | | Temporarily restricted contributions | Contribution receivable |
| Palestinian Agricultural Relief Committee (PARC) – Donated equity | 800,000 | - | - | - | - | 800,000 | - |
| European Commission (EC) | 332,662 | - | - | (282,594) | (12,984) | 37,084 | - |
| Spanish Agency for International Development Cooperation (AECID) | 137,561 | - | - | (137,561) | - | - | - |
| Institution strengthening Reef Finance Co.- Netherland | 481,205 | - | 1,397,269 | (1,530,976) | - | 347,498 | - |
| Declining Musharakeh - UNDP | 100,000 | - | - | - | - | 100,000 | - |
| UNDP - Deep Al Qard Al Hassan | - | - | 85,000 | (28,800) | - | 56,200 | - |
| UNDP – Deep | - | (2,542) | 4,000 | (1,458) | - | - | - |
| | 1,851,428 | (2,542) | 1,486,269 | (1,981,389) | (12,984) | 1,340,782 | - |

REEF FINANCE COMPANY (NOT FOR PROFIT)

Financial statements for the year ended December 31, 2012

NOTES TO THE FINANCIAL STATEMENTS

(All amounts are in US Dollar)

NOTE (9) OTHER CURRENT ASSETS

Details:

| | <u>2012</u> | <u>2011</u> |
|--------------------------------------|----------------------|----------------------|
| Due from employees | 41,637 | 20,439 |
| Interest receivable on granted loans | 21,549 | 32,509 |
| Prepaid expenses | 14,819 | 19,306 |
| | <u>78,005</u> | <u>72,254</u> |

NOTE (10) CASH AND CASH EQUIVALENTS

Details:

| | <u>2012</u> | <u>2011</u> |
|----------------------------|-------------------------|-------------------------|
| Cash on hand | 11,712 | 40,730 |
| Cash at banks | 1,009,214 | 2,641,245 |
| Term deposits at banks (*) | 257,365 | 518,270 |
| | <u>1,278,291</u> | <u>3,200,245</u> |

(*) these represent short term deposits that mature within one month of placement and bear interest in the range of 0.5%-2% per annum.

NOTE (11) SHARE CAPITAL

As of January 1, 2012, the share capital amounted to USD 195,500 which is fully paid. An additional amount USD 4,500 was settled by the shareholders during the year 2012.

NOTE (12) SUBORDINATE LOAN

Based on the signed agreement between Palestinian Agricultural Relief Committees (PARC) and Reef, as of September 10, 2007, and later discussions, PARC agreed to transfer USD 1,500,000 for Reef to be used for granting loans. During the years 2008 and 2009, Reef received from PARC the total agreement amount of USD 1,500,000. The amount was disbursed as loans during 2008 and 2009.

The amount received was booked as a subordinate loan, based on the intent of PARC to transfer the amount granted to capital by December 31, 2012. During the year 2012, the Board of Directors approved the transfer of the amount to capital once registered by the company registrar.

NOTE (13) LONG TERM LOANS

Details:

| | <u>2012</u> | <u>2011</u> |
|--|-------------------------|-------------------------|
| Matures over one year and less than five years | 667,008 | 1,333,257 |
| Matures during next year | 552,444 | 433,096 |
| | <u>1,219,452</u> | <u>1,766,353</u> |

Movement of long term loans as follows:

| | <u>Beginning balance</u> | <u>Borrowings</u> | <u>Repayments</u> | <u>Ending balance</u> |
|-----------------|------------------------------|-------------------|-------------------|-----------------------|
| Long term loans | 1,766,353 | - | (546,901) | 1,219,452 |

REEF FINANCE COMPANY (NOT FOR PROFIT)

Financial statements for the year ended December 31, 2012

NOTES TO THE FINANCIAL STATEMENTS

(All amounts are in US Dollar)

NOTE (14) PROVISION FOR EMPLOYEES' INDEMNITY

Details:

| | <u>Beginning Balance</u> | <u>Additions during the year</u> | <u>Payments during the year</u> | <u>Ending balances</u> |
|------------------------------------|------------------------------|--|---|----------------------------|
| Employees' end of service benefits | 84,493 | 36,763 | (17,638) | 103,618 |
| Provident fund | 119,907 | 48,748 | (28,625) | 140,030 |
| | <u>204,400</u> | <u>85,511</u> | <u>(46,263)</u> | <u>243,648</u> |

NOTE (15) CASH MARGINS

This amount represents the balance of cash margins deposited by borrowers' collateral for the granted loans. These cash margins are deposited in local banks and are reviewed on a monthly basis.

NOTE (16) PAYABLES AND ACCRUALS

Details:

| | <u>2012</u> | <u>2011</u> |
|---------------------|---------------|---------------|
| Accounts payable | 14,760 | 8,691 |
| Interest payable | 5,500 | 8,022 |
| Accrued expenses | 23,931 | 6,452 |
| Refundable fees | - | 4,849 |
| Payroll tax payable | 5,406 | 3,696 |
| | <u>49,597</u> | <u>31,710</u> |

NOTE (17) FINANCING INCOME AND COMMISSION

Details:

| | <u>2012</u> | <u>2011</u> |
|--|----------------|----------------|
| Financing income | 617,012 | 448,796 |
| Morabaha income collected on the date of the transaction | 154,048 | 57,331 |
| | <u>771,060</u> | <u>506,127</u> |
| Commission | 2,424 | 50,386 |
| | <u>773,484</u> | <u>556,513</u> |

REEF FINANCE COMPANY (NOT FOR PROFIT)

Financial statements for the year ended December 31, 2012

NOTES TO THE FINANCIAL STATEMENTS

(All amounts are in US Dollar)

NOTE (18) GENERAL AND ADMINISTRATIVE EXPENSES

Details:

| | 2012 | | 2011 | | Total | |
|-----------------------------------|----------------|----------------|----------------|----------------|----------------|----------------|
| | Administrative | Projects | Administrative | Projects | 2012 | 2011 |
| Salaries and related benefits (*) | 426,079 | 111,535 | 310,028 | 202,751 | 537,614 | 512,779 |
| Advertisement | 944 | 38,163 | 22,931 | 19,488 | 39,107 | 42,419 |
| Rent | 35,513 | 11,705 | 20,131 | 21,517 | 47,218 | 41,648 |
| Utilities | 22,700 | 5,898 | 14,097 | 18,677 | 28,598 | 32,774 |
| Research fees | - | - | - | 29,871 | - | 29,871 |
| Professional fees | 52,234 | 3,785 | 25,139 | 4,578 | 56,019 | 29,717 |
| Work shop expense | - | - | - | 23,400 | - | 23,400 |
| Transportation | 28,883 | 200 | 20,531 | 1,200 | 29,083 | 21,731 |
| Maintenances | 15,007 | - | 12,552 | 8,700 | 15,007 | 21,252 |
| Stationary and office supplies | 6,828 | 2,668 | 5,048 | 6,677 | 9,496 | 11,725 |
| Public relation expenses | - | - | 881 | 10,305 | - | 11,186 |
| Subscription | 6,099 | - | 10,616 | - | 6,099 | 10,616 |
| Travel expense | 12,701 | 2,753 | 6,959 | 3,510 | 15,454 | 10,469 |
| Other | 4,770 | 15,599 | - | 9,214 | 20,369 | 9,214 |
| Training fees | 13,265 | 10,741 | - | 7,603 | 24,006 | 7,603 |
| Hospitality | 6,570 | - | 7,297 | - | 6,570 | 7,297 |
| Fuel expenses | 2,808 | - | 4,926 | - | 2,808 | 4,926 |
| Entertainments | 2,120 | - | 1,900 | - | 2,120 | 1,900 |
| General insurance | 1,580 | - | 1,781 | - | 1,580 | 1,781 |
| | 638,101 | 203,047 | 464,817 | 367,491 | 841,148 | 832,308 |

(*) Details of salaries and related benefits are as follows:

| | 2012 | 2011 |
|---------------------------------|----------------|----------------|
| Salaries and related allowances | 432,058 | 439,519 |
| End of service expense | 36,763 | 30,934 |
| Provident fund expense | 32,499 | 30,444 |
| Employees health insurance | 11,044 | 9,675 |
| Rewards expense | 25,250 | 2,207 |
| | 537,614 | 512,779 |

REEF FINANCE COMPANY (NOT FOR PROFIT)

Financial statements for the year ended December 31, 2012

NOTES TO THE FINANCIAL STATEMENTS

(All amounts are in US Dollar)

NOTE (19) FINANCE EXPENSES

Details:

| | <u>2012</u> | <u>2011</u> |
|-------------------------------|----------------------|----------------------|
| Currency variance loss/(gain) | 2,944 | (3,372) |
| Interest on loans | 16,569 | 25,186 |
| Bank commissions and charges | 47,359 | 14,417 |
| | <u>66,872</u> | <u>36,231</u> |

NOTE (20) RELATED PARTIES

Related parties represent associated entities, shareholders, directors and key management personnel of the company, and entities controlled, jointly controlled or significantly influenced by such parties.

| | <u>Relation</u> | <u>2012</u> | <u>2011</u> |
|---------------------------------------|-----------------|-------------|-------------|
| Key management personnel compensation | Key management | 59,683 | 57,028 |
| End of service benefits | Key management | 4,115 | 4,115 |

NOTE (21) SUBSEQUENT EVENTS

On March 24, 2013, during the General Assembly meeting referenced (2/2013), management decided to raise the paid in capital of Reef to USD 5,000,000. This increase is expected to be settled during the six months after the aforementioned meeting.

NOTE (22) RESTATEMENT OF FINANCIAL STATEMENTS

During the year 2012, Reef changed its policy in respect of accounting for Morabaha profits collected on the date of transaction. Under the new policy, the income generated from the aforementioned is recognized immediately on the date on each transaction. Under the previous policy, Reef deferred the collected amount and accounted it under the liabilities section.

Management has restated the comparative figures (i.e. 2011) to comply with the new policy. The details of the change are as follows:

Statement of income and other comprehensive income

| | <u>As restated</u> | <u>Before</u> | <u>Net change</u> |
|--|-----------------------|-----------------------|----------------------|
| | <u>2011</u> | <u>restatement</u> | |
| | | <u>2011</u> | |
| Financing income | 448,796 | 448,796 | - |
| Morabaha income collected on the date of the transaction | 57,331 | - | 57,331 |
| | <u>506,127</u> | <u>448,796</u> | <u>57,331</u> |

Statement of financial position

| | <u>As restated</u> | <u>Before</u> | <u>Net change</u> |
|----------------------------|--------------------|----------------------|------------------------|
| | <u>2011</u> | <u>restatement</u> | |
| | | <u>2011</u> | |
| Deferred interest revenues | - | 347,409 | (347,409) |
| Prior period adjustment | - | (290,078) | 290,078 |
| | <u>-</u> | <u>57,331</u> | <u>(57,331)</u> |

NOTE (23) COMPARATIVE FIGURES

The corresponding figures of December 31, 2011 have been reclassified in order to conform to the presentation for the current year. Except for the adjustments explained in note 22, such reclassifications do not affect previously reported net assets.