



PEC

PALESTINE  
ELECTRIC  
COMPANY

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ANNUAL REPORT  
2011

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*The Positive Power  
of Giving Light*



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# PALESTINE ELECTRIC COMPANY

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## CHAIRMAN'S Insights for 2011/2012





**Said Khoury - Chairman**

Dear Shareholders

Another year passes as we find ourselves, once again, proudly assembled in conveyance of our appreciation for the continued support of our shareholders and the faith of the Palestinian people in our ability to fulfill our responsibilities.

As a proud and devoted Palestinian, one of the dearest projects to my heart is the 'Palestine Electric Company'. While this company's function is to supply the demands for electric power and it is a well-performing investment, its greatest by-product is that it actively and effectively provides a better life and more positive future to Palestinians.

Palestine Electric Company (PEC) was established on the strong basis of playing a positive role in the economy and community. We strive to continuously uphold the highest standards in professionalism, efficiency, management practices, and always meet our shareholders' expectations. With our achievements in 2011, I can proudly say that the strong foundation of this company and the support of our shareholders lay out a positive outlook for the future of PEC.

As the prime developer in the West Bank power generating plant, we are ready to take on 2012 with high spirits, ensuring that the returns of our shareholders are secured and in safe hands.

A handwritten signature in blue ink, appearing to read 'S. Khoury', with a stylized flourish at the end.

Said Khoury  
Chairman



## EXECUTIVE MANAGING DIRECTOR'S Letter





**Walid Salman - Executive Managing Director**

To our Shareholders

As the years pass by, I am proud that our company is performing all of its duties and meeting all its obligations, technically and financially, without exception. Palestine Electric Company is also achieving the expected financial returns and advancing in its mission in light of the difficult situation in our country and in the electricity sector in Gaza.

Palestine Electric Company is developing its technical skills and enhancing its investment portfolio in order to expand within the Palestinian electricity sector.

We succeeded in expanding to the West Bank and have signed the necessary agreements with the Palestine Energy and Natural Resources Authority (PENRA), to establish a new power generating company in the West Bank. Palestine Electric Company is the main developer and owns the majority shares in this new project, thus benefiting from the accumulated knowledge base and successes that Palestine Electric Company has achieved.

We assure our shareholders that we are moving forwards in order to continually develop and enhance the performance of our company and our financial returns on the capital investment, for the benefit of our shareholders, the Palestinians and Palestine. We are confidently moving along the road to success with your support and trust.


The financial results for our company for the year 2011 were relatively better and more positive than our year 2010 results thus confirming our strong financial position and assuring that we are on the right path.

A handwritten signature in black ink, appearing to be 'W. Salman'.

Walid Salman  
Executive Managing Director



## EXECUTIVE SUMMARY - 1. Company Brief



PEC was established in 1999 in accordance with Palestinian laws, to establish and operate power generating plants in Palestinian territories.

We are a public owned company whereby the public shareholders represent 33% and the private shareholders represent 67%.

Gaza Power Generating Company (GPGC) was established as the power plant's operational arm with a capital of \$60 million.

Palestine Electric Company owns GPGC, the sole Palestinian supplier of power in Gaza, based on the signed agreements.

## PEC's Timeline

**1999**

- Establishment of the Palestine Electric Company P.L.C

**2004**

- Commercial Operation of the power plant at 140 MW
- First General Assembly Meeting conducted
- Started Trading on the Palestine Securities Exchange

**2005**

- First dividend distribution to shareholders

**2006**

- Air attack targeted the power plant transformers in June
- PEC Shares suspended from trading to protect the shareholders - Returned to normal trading Nov.
- Re-Operation of the power plant commenced in October

**2007**

- Main maintenance of the power plant done
- Installation of the final transformer as part of the repairing work, post 2006 events

**2009**

- Finalised all main maintenance work for turbines and ensured safe operations

**2010**

- Establishment of Palestine Power Generating Company in the West bank in collaboration with partners and investors from a consortium of sectors in Palestine

**2011**

- Conclusion of the periodic maintenance work by Seimens for one of the gas and steam turbines at the end of 2011
- Launched the community development section POSITIVE, which supports all non-profit humanitarian organisations and encourages community work at all levels.

## PEC & the Environment

We aim to ensure that the plant is operated and maintained in an environmentally sensitive manner and in accordance with applicable OPIC requirements, World Bank guidelines and local Palestinian environmental requirements and policies.

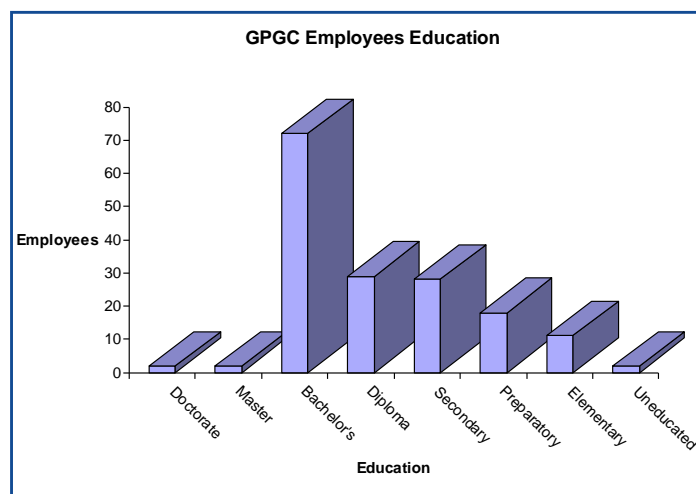


## Our Employees

The Company conducts regular training updates, evaluations and developments for the employees, and Policies and procedures have been established to maintain employee work standards, professionalism and to maintain that the staff are always up to par in all technological advances over the years.

The Company currently employs 164 staff divided into administration, engineering, technical and security workers. These employees have all acquired the appropriate degrees and certifications for their posts as follows:

2 employees:	PHD
2 employees:	Masters Degree
72 employees:	Bachelors Degree
10 employees:	Diplomas
19 employees:	Technical certificates
11-18-28 employees:	Primary, Elementary and/or High school
2 employees:	no certificates



The company has succeeded in employing a Palestinian workforce in all its technical and managerial departments.



## Power Generating Plant: Operations & Technical Summary

The Gaza power plant of 140MW capacity was originally designed to fulfill the power needs of the Gaza governorates taking into considerations the industrial needs and the natural population growth.

The power plant operates in a combined cycle based on four Gas Turbines and two Steam Turbines in a configuration of two blocks. The turbines are designed to allow for dual fuel system and could burn both natural gas and fossil fuel.

The infrastructure design was flexible enough to allow for the expansion of the power plant in the future and the increase of the production capacity. But since the commissioning of the power plant, we are still promised, by the Palestine Energy & Natural Resources Authority (PENRA), the expansion in the local grid to absorb the full production capacity of the power plant.

The Israeli bombing of the plant transformers in 2006 led to the reduction of the power that can be absorbed by the PENRA due to the limitations of the substituted transformers relative to the original transformers.

PENRA is in the process of procuring an additional number of transformers to be commissioned by mid 2012. The new addition would enable PENRA to evacuate the full capacity of the power plant.

Since the power plant turbines could burn both natural gas and fossil fuel, Palestine Electric Company management continually encourages the Palestinian Authority to enhance its efforts in trying to supply natural gas to the power plant thus increasing efficiency and resulting in cost savings to the consumer.



## 2. Board of Directors & Executive Management

### Executive Management

**Walid Salman**

Member of the Board of Directors,  
Executive Managing Director

**Rafiq Maliha**  
**Mohammad Sherif**  
**Mahmoud Nabahin**

Senior Technical Manager  
Plant Manager  
Financial Manager

## PEC Board of Directors

#	Names	Position	Representative	Address
1	Said Khoury	Chairman		
2	Shukri Bishara	Vice Chairman		
3	Mohamed Mustafa	Member		
4	Tarek Aqqad	Member	Palestine Power Company	Gaza, Al Nusirat, Salah Al Din St., Power Plant, P.O Box 1336, Tel 2888600, Ext # 331, Fax 2888607
5	Nabil Sarraf	Member		
6	Hani Ali	Member		
7	Marwan Salloum	Member		
8	Sharhabeel Al Zaeem	Member		
9	Walid Salman	Member	Palestine Electric Company Holding	Gaza, Al Nusirat, Salah Al Din St., Power Plant, P.O Box 1336, Tel 2888600, Ext # 331, Fax 2888607
10	Samir Shawwa	Member		
11	Faisal Shawwa	Member	Morganti Development LLC	Jordan, Amman, P.O Box 830392, tel +9626 4658403, fax +9626 4643071
12	Khaled Osaily	Member		
13	Farouq Franji	Member	Insurance & Pension General Corp.	Gaza, Al Remal, Thourah St., Tel 2829219, Fax 2822473
14	Iyad Basal	Member	Public Shareholder	Gaza, Al Remal, Haifa St., Tel. 2848025, Telefax 2840384

*\*According to the company's Articles of Association, three seats on the Board of Directors are dedicated to any Public Shareholders holding 1% or more of the shares. At the time of this report, only two seats have been occupied and an exemption has been granted due to the lack of any others holding the required amount of shares or willingness to hold a seat on the Board of Directors.*

## Board of Directors Meetings During 2011

A Board of Directors Meeting was held on 27 April 2011, preceding the General Assembly Meeting in which the Board of Directors agreed to recommended to the General Assembly a dividend declaration and payout of an amount equivalent to 10% of the company's original capital to the shareholders owning shares up to the day of the General Assembly Meeting. This was approved by the General Assembly.

## General Assembly Meeting Date

The assigned date for holding our General Assembly Meeting for 2011 is: Wednesday 25 April 2012.

### 3. Company Auditors & Legal Advisors



#### External Auditors for 2011

Following the voting of the last General Assembly Meeting, Ernst & Young have been appointed as the company's external auditors for the year 2011.

#### Company Legal Advisor

Sharhabeel Al Zaeem & Associates

### 4. Standards of Work Conduct

#### Transparency

Since the listing of PEC in the Palestine Exchange (PEX), we have implemented a continuously transparent policy in declaring all requested information in parallel to the local regulations of the PEX. It is essential for us to maintain a close relationship with our shareholders and investors and to present to them all the information necessary to make sound and studied decisions on their investments and share purchasing.

#### Legality

Palestine Electric Company does not have any past or ongoing legal case raised by or upon it.



## 5. Investor Relations & Community Work

### The Investor Relations Department - Dividend Distribution

The development of the Investor Relations Department started in 2005 and PEC was one of the first companies trading in the Palestine Exchange to develop a specific department that deals with all shareholders concerns and issues.

The company ensures that the rights of its shareholders are protected and any uncollected dividends remain within the company reserves for payment to the shareholders upon presenting their proper claims.

### Shareholders Information Mechanism

Shareholders receive our information via the Palestine Securities Exchange and the Capital Market Authority in addition to our website. Our Annual Report is always available to shareholders two weeks prior to the annual meeting date, and can be obtained from Gaza, Ramallah, and Nablus (we place newspaper advertisements with details of the locations).

### PEC's Role in the Community

In 2011, the company launched a new section under the Investor Relations Department called POSITIVE. Positive supports humanitarian organisations and encourages community work on all levels.

PEC is always on the lookout to support seminars, conferences and summits in Palestine that help in shedding light on detrimental issues in the country from science and technology to finance and statistics.

**Humanitarian Aid:** PEC always tries to reach families in need of urgent financial/medical aid. The company also organizes, on an annual basis, the distribution of food baskets to a list of families in need.

**Corporate Social Responsibility:** In alignment to our mission, we aim to aid and benefit our community through various outlets. Working alongside educational facilities, Palestinian establishments, schools, universities, and training programs is one of those outlets. By introducing students, specialists, and our local youth to our Plant, we are sharing knowledge with our community and allowing for a mutual sense of responsibility in sustaining a state-of-the-art Palestinian operated Power Plant. Engineers & Students alike will be able to gain visual experience of the systems that go into operating a plant.

### Our Information Technology

Palestine Electric Company has devoted a considerable amount of its resources in making sure we are always up to par with our IT standards and applications internally and externally.

During 2011, the IT department worked on developing a new website, "the portal Gate", in order to digitize, archive, simplify and adapt to a new and fast changing global IT environment. We have created our own archiving and follow up software utilizing the latest web technology, and added many features to minimize the error percentage and provide reliable and faster services for all GPGC departments. Our goal is to minimize the amount of paper consumption and by 2012 we aim at completely eliminating unnecessary paper usage thus becoming more environmentally friendly.

In addition to the above, the IT department has also upgraded and modified the PEC website using the latest web technology, making it more user friendly in order to further encourage transparent and efficient communication with our shareholders and investors.

## 6. The West Bank Expansion & Future Plans

After 9 years of experience in operating and maintaining the Gaza power plant, we have decided to participate in the establishment and development of a power generating company in the West Bank.

During 2010, all the necessary documents for the establishment of the new West Bank power plant (Palestine Power Generating Company PLC) have been signed with the Palestinian Energy & Natural Resources Authority (PENRA). We are ready to embark on this important project as the main developer.

Our technical, professional and managerial development along the years will help us prove our sustainability across Palestine and outside Palestine.

**The Gaza Strip and West Bank**



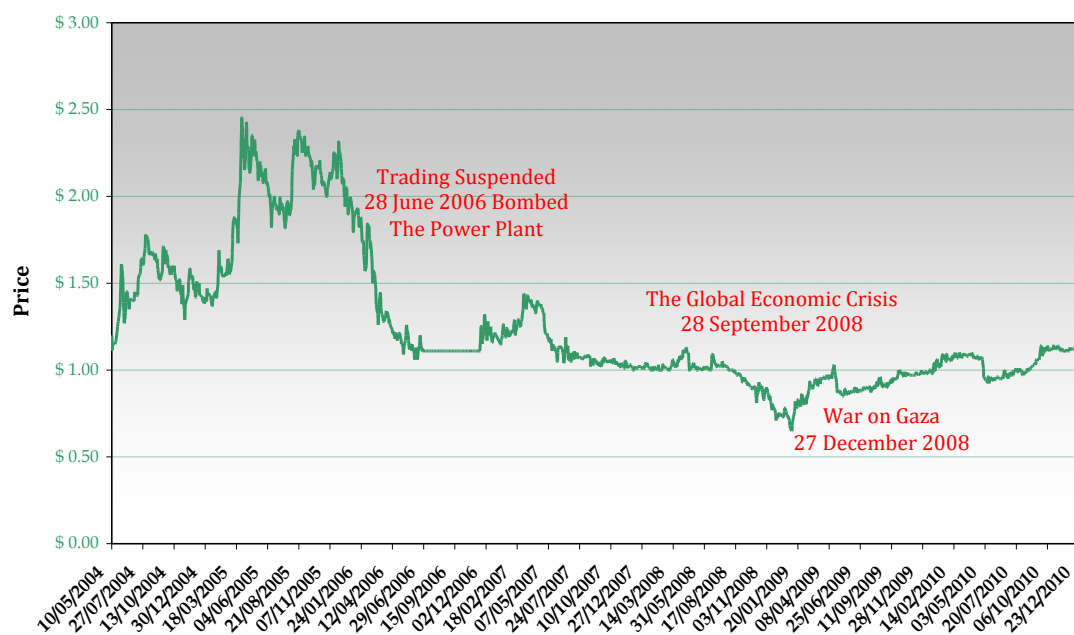
## 7. Shareholders

Shareholder/s owning more than 5% of the PEC shares:		
Name of Company	Number of Shares	Rate
Palestine Power Company	38,999,600	65 %

Analysis of registered holdings for 2010-2011						
Distribution of shares by type of shareholder	Number of holdings		Shares		Rate	
Year	2010	2011	2010	2011	2010	2011
Institutional investors	5	5	40,200,000	40,200,000	% 67.00	% 67.00
Individuals	11,857	11,654	19,800,000	19,800,000	% 33.00	% 33.00
Total	11,862	11,659	60,000,000	60,000,000	% 100	% 100
Range analysis of register	Number of holdings		Shares		Rate	
Year	2010	2011	2010	2011	2010	2011
1 – 500	3,357	3,330	1,094,613	1,077,393	% 1.82	% 1.80
501 – 1 000	5,857	5,726	4,224,278	4,135,275	% 7.04	% 6.89
1 001 – 5 000	2,307	2,262	3,911,653	3,877,930	% 6.52	% 6.46
5 001 – 10 000	165	160	1,150,629	1,134,577	% 1.92	% 1.89
10 001 – 50 000	134	143	2,925,465	3,094,483	% 4.88	% 5.16
50 001 – 100 000	21	13	1,555,597	971,343	% 2.59	% 1.62
100 001 – 1 000 000	20	24	6,138,165	6,709,399	% 10.23	% 11.18
1 000 001 and above	1	1	38,999,600	38,999,600	% 65.00	% 65.00
Total	11,862	11,659	60,000,000	60,000,000	% 100	% 100

## 8. PEC Share Performance

### PEC Share Price 2004-2010



PEC Share all time high \$2.45 year 2005

PEC Share all time low \$0.65 year 2009

PEC Share 2011 high \$1.25

### PEC Share Statistics 2011

Opening Price	Closing Price	High	Low	Trading Volume	Shares Traded	Number of Deals
\$1.13	\$1.19	\$1.25	\$1.06	\$2,598,368	2,237,178 shares	1,589 deals

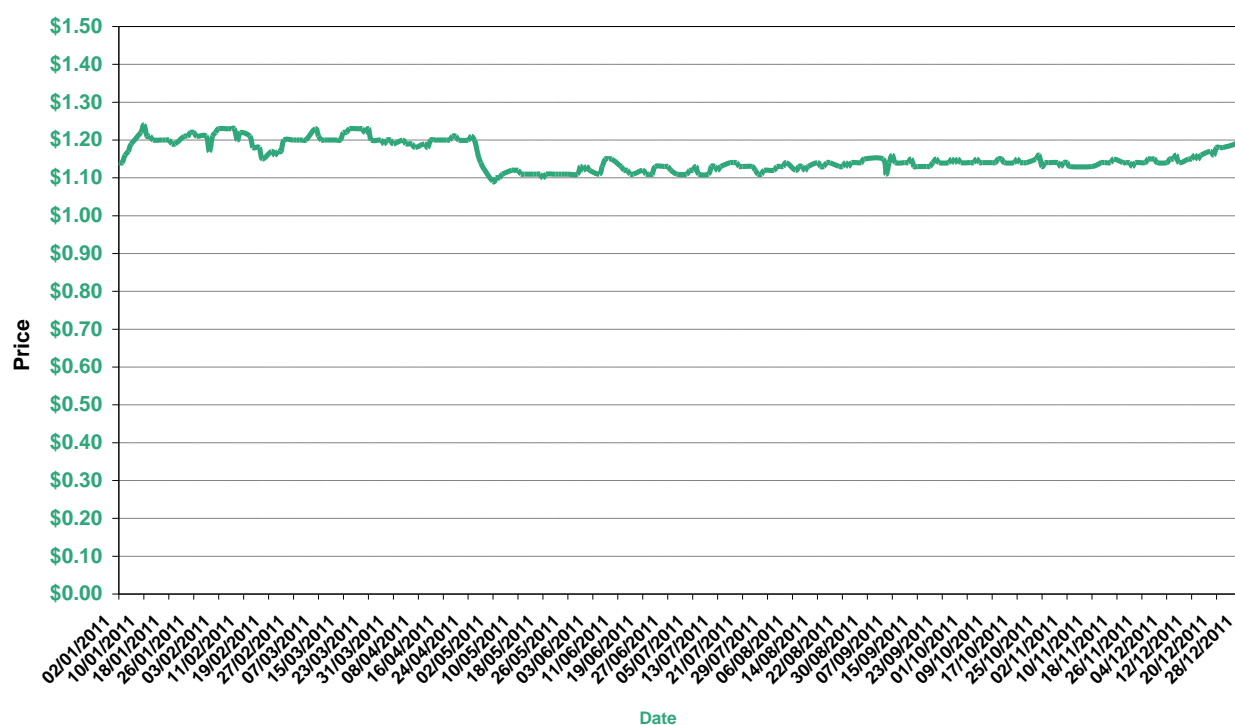
### Corporate Governance

The Company's Board of Directors maintains the security of the shareholders rights by continuously enhancing the company policies and procedures and its performance in addition to safeguarding the Company assets. The Board of Directors also direct the executive management of the Company to take the necessary steps in enhancing the shareholders value. In addition to the above, the Board ensures the implementation of policies and procedures that allows for the enforceability of a Corporate Governance in line with International and best practices standards.

### PEC shares relative to Al Quds Index

The PEC share and all shares trading on the Palestine Exchange are affected by the political and economic situation in Palestine. Nonetheless, PEC shares have received a lot of support and trust from shareholders thus allowing it to settle around a relatively good and stable price.

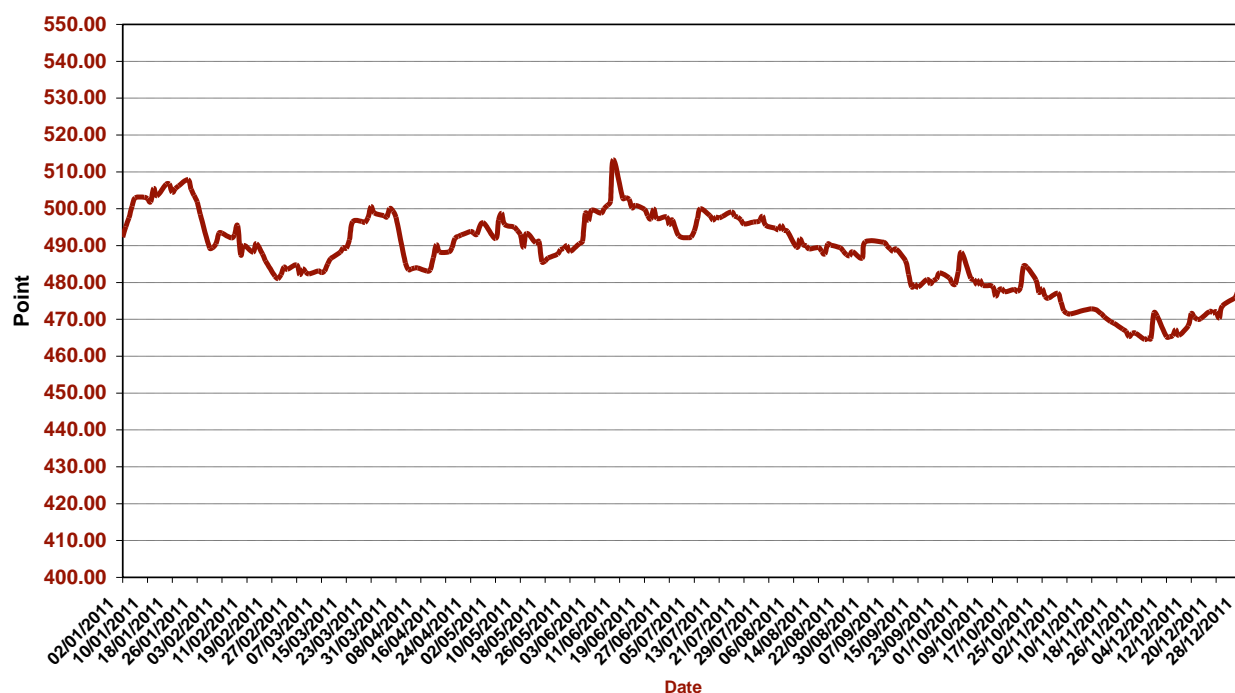
## PEC share price 2011



In comparison with Al Quds index, which closed at a low in the year-end, PEC share price closed at a high in the last quarter even thou the majority of trading companies went down and effected Al Quds index.

PEC Shares are one of the 15 selected sample group shares for the statistical calculations of the Al Quds index in the Palestine Exchange (PEX) which follows international standards and laws in its calculations.

## Al Quds Index 2011



# COMMENTS ON FINANCIAL RESULTS

## Financial Results for 2011

The Company financial results for 2011 are very promising, relative to 2010, thus confirming our strong financial position and is assuring to shareholders that we are on the right track.

The 2011 financial results show an improvement in our performance reflecting a strong company with a professional working team and effective management.

## In Numbers

Details	2007	2008	2009	2010	2011
Net Profit	\$ 4,355,802	\$ 6,278,138	\$ 6,983,424	\$ 6,782,383	\$ 8,374,034
Total Equity	\$ 71,324,831	\$ 74,002,969	\$ 74,986,394	\$ 75,768,777	\$ 78,142,811
PEC Share Price	\$ 1.01	\$ 0.68	\$ 1.04	\$ 1.14	\$ 1.19
Dividends Distributions	\$ 3,600,000	\$ 6,000,000	\$ 6,000,000	\$ 6,000,000	-
Rate of Dividends Distributions	6%	10%	10%	10%	-

## Difference between Preliminary Financial Results and Audited Financial Results for 2011

General Ledger Account	Audited Financial Statements	Preliminary Financial Statements	Difference	Reason
Other Current Assets	\$4,671,456	\$3,614,425	\$1,057,031	Reclassification of accounts
Other Current Liabilities	\$15,340,350	\$14,283,319	\$1,057,031	Reclassification of accounts

## Distribution of Cash Dividends

During the past years, the company has succeeded in declaring and paying out dividends to its shareholders despite the unstable political and economic situation within the area.

Our financial position for 2011 is good and is promising for the future of this company. It is our goal to stand by our vision of maximising our shareholders' value by continuously striving to develop and expand our capabilities while balancing out the uncertainties of the political and economical environment.

## Board of Directors Remuneration

The Board of Director have agreed, during their meeting on 27 April 2011, to pay the below rewards and remunerations for the Board members for the year 2010.

#	BOD	\$ Value
1	Palestine Power Company	79,900 \$
2	Palestine Electric Company Holding	28,200 \$
3	Morganti Development LLC	28,200 \$
4	Public Shareholder - Palestine Pension Fund	14,100 \$
5	Public Shareholder - Iyad Basal	14,100 \$
Total		164,500 \$

## Financial Summary 2010-2011

Financial Ratios	2010	2011
Turnover Share	0.041	0.037
Earnings per Share	0.113	0.140
Book Value per Share	1.263	1.302
Market Value to Book Value (One Time)	0.903	0.914
Equity Ratio	0.608	0.664
Return on Equity	0.090	0.107

## Budget for 2012

The Company's budget focus for 2012 is mainly targeted towards the management of its operational and contractual obligations.

The Company's strategy for 2012 is in line with previous endeavors of allocating a portion of the company budget towards carrying out key functions to support the strategic development of the company.

Our main target for the coming year is to invest in the development of a power generating company in the West Bank, backed up by our expertise in this sector.



Palestine Electric Company  
Public Shareholding Company Limited

Consolidated Financial Statements  
December 31, 2011

## **Independent Auditors' Report to the Shareholders of Palestine Electric Company - Public Shareholding Company Limited**

We have audited the accompanying consolidated financial statements of Palestine Electric Company - Public Shareholding Company Limited (the Company), which comprise the consolidated statement of financial position as of December 31, 2011 and the consolidated statement of income and comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

### **Board of Directors' Responsibility for the Financial Statements**

The Board of Directors is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditors' Responsibility**

Our responsibility is to express an opinion on these consolidated 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 about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated financial statements.

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

### **Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2011 and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

**Emphasis of Matters**

Without qualifying our opinion, as explained in note (9) to the accompanying consolidated financial statements, the Palestinian Energy and Natural Resources Authority (PENRA) is the sole customer of the Company. To the date of the issuance of this report, PENRA did not provide the Company with the letter of credit as required by the power purchase agreement. In addition, as explained in note (10) to the accompanying consolidated financial statements, to the date of issuance of this report, the two remaining step-up transformers PENRA is committed to supply and install have not been supplied nor installed. PENRA did however make a commitment to supply and install these two transformers as soon as the situation in Gaza permits.

Furthermore, as explained in note (28) to the accompanying consolidated financial statements, the Company's assets which mainly comprise property, plant and equipment are located in Gaza. Recoverability of these assets from the Company's operations depends on the stabilization of the political and economic situation in Gaza.



March 8, 2012  
Gaza, Palestine

# **CONSOLIDATED STATEMENT OF FINANCIAL POSITION**

As at December 31, 2011

	Notes	2011 U. \$. \$	2010 U.S. \$
<b>ASSETS</b>			
<b>Non-current assets</b>			
Property, plant and equipment	4	76,873,504	83,796,560
Intangible asset	5	1,587,584	1,717,184
Prepayments	6	-	306,575
Investment in an associate	7	1,008,805	112,577
		<u>79,469,893</u>	<u>85,932,896</u>
<b>Current assets</b>			
Materials and inventories	8	6,592,855	6,266,548
Accounts receivable	9	20,053,040	22,638,192
Other current assets	10	4,671,456	3,819,063
Cash and bank accounts	11	6,939,668	5,893,895
		<u>38,257,019</u>	<u>38,617,698</u>
<b>TOTAL ASSETS</b>		<u>117,726,912</u>	<u>124,550,594</u>
<b>EQUITY AND LIABILITIES</b>			
<b>Equity</b>			
Paid-in share capital	12	60,000,000	60,000,000
Statutory reserve	13	6,891,759	6,054,356
Retained earnings		<u>11,251,052</u>	<u>9,714,421</u>
<b>Total equity</b>		<u>78,142,811</u>	<u>75,768,777</u>
<b>Non-current liabilities</b>			
Long term loans	14	17,973,393	21,942,000
Provision for employees' indemnity	15	1,920,358	1,795,186
Credit facilities mature after a year	16	<u>2,849,000</u>	<u>-</u>
		<u>22,742,751</u>	<u>23,737,186</u>
<b>Current liabilities</b>			
Current portion of long term loan	14	-	18,603,000
Credit facilities mature within a year	16	1,501,000	-
Other current liabilities	17	<u>15,340,350</u>	<u>6,441,631</u>
		<u>16,841,350</u>	<u>25,044,631</u>
<b>Total liabilities</b>		<u>39,584,101</u>	<u>48,781,817</u>
<b>TOTAL EQUITY AND LIABILITIES</b>		<u>117,726,912</u>	<u>124,550,594</u>

The attached notes 1 to 28 form part of these consolidated financial statements

**CONSOLIDATED STATEMENT OF INCOME AND COMPREHENSIVE INCOME**  
Year Ended December 31, 2011

	Notes	2011 U.S. \$	2010 U.S. \$
<b>Revenues</b>			
Capacity charges	18	29,890,896	29,622,024
Operating expenses	19	(21,359,984) 8,530,912	(21,957,729) 7,664,295
Interest on PENRA's receivables		963,832	490,128
Force majeure government assistance	20	-	6,676,569
Finance costs		(1,220,849)	(1,558,298)
Impairment of accounts receivable	9	-	(6,756,132)
Share of results of an associate	7	(218,772)	(92,423)
Other revenues		318,911	358,244
<b>Profit for the year</b>		8,374,034	6,782,383
Other comprehensive income		-	-
<b>Total comprehensive income for the year</b>		8,374,034	6,782,383
Basic and diluted earnings per share	21	0.14	0.11

**CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**  
Year Ended December 31, 2011

	Paid-in Share Capital	Statutory Reserve	Retained Earnings	Total Equity
	U.S. \$	U.S. \$	U.S. \$	U.S. \$
<b>2011</b>				
Balance at January 1, 2011	60,000,000	6,054,356	9,714,421	75,768,777
Total comprehensive income for the year	-	-	8,374,034	8,374,034
Transfer to statutory reserve	-	837,403	(837,403)	-
Dividends (note 22)	-	-	(6,000,000)	(6,000,000)
<b>Balance at December 31, 2011</b>	<b>60,000,000</b>	<b>6,891,759</b>	<b>11,251,052</b>	<b>78,142,811</b>
<b>2010</b>				
Balance at January 1, 2010	60,000,000	5,376,118	9,610,276	74,986,394
Total comprehensive income for the year	-	-	6,782,383	6,782,383
Transfer to statutory reserve	-	678,238	(678,238)	-
Dividends (note 22)	-	-	(6,000,000)	(6,000,000)
<b>Balance at December 31, 2010</b>	<b>60,000,000</b>	<b>6,054,356</b>	<b>9,714,421</b>	<b>75,768,777</b>

**CONSOLIDATED STATEMENT OF CASH FLOWS**  
Year Ended December 31, 2011

	2011 U.S. \$	2010 U.S. \$
<b><u>Operating activities</u></b>		
Profit for the year	8,374,034	6,782,383
Adjustments:		
Provision for employees' indemnity	246,222	413,058
Depreciation of property, plant and equipment	6,943,628	6,958,822
Amortization	271,263	271,267
Finance costs	1,220,849	1,558,298
Impairment of accounts receivable	-	6,756,132
Share of results of an associate	218,772	92,423
	17,274,768	22,832,383
<b><u>Working capital adjustments:</u></b>		
Accounts receivable	2,585,152	(19,751,988)
Other current assets	(852,393)	2,910,545
Materials and inventories	(326,307)	(997,159)
Other current liabilities	4,260,336	(5,382,472)
Employees' indemnity paid	(121,050)	(25,844)
<b>Net cash flows from (used in) operating activities</b>	22,820,506	(414,535)
<b><u>Investing activities</u></b>		
Purchase of property, plant and equipment	(20,572)	(22,623)
Purchase of investment in an associate	(1,115,000)	(205,000)
<b>Net cash flows used in investing activities</b>	(1,135,572)	(227,623)
<b><u>Financing activities</u></b>		
Long term loan	11,000,000	-
Loan repayment	(33,571,607)	(6,003,000)
Credit facilities	4,350,000	-
Finance cost paid	(862,386)	(656,080)
Dividends paid	(1,555,168)	(5,816,034)
<b>Net cash flows used in financing activities</b>	(20,639,161)	(12,475,114)
<b>Increase (decrease) in cash and cash equivalents</b>	1,045,773	(13,117,272)
Cash and cash equivalents at January 1	5,893,895	19,011,167
<b>Cash and cash equivalents at December 31</b>	6,939,668	5,893,895

The attached notes 1 to 28 form part of these consolidated financial statements

## **NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2011

### **1. General**

Palestine Electric Company - Public Shareholding Company Limited (the Company) located in Gaza - Palestine was established and registered in Gaza on December 14, 1999, under registration number (563200971) in accordance with the Companies' Law of 1929.

The main objectives of the Company are to establish electricity generating plants in the territories of the Palestinian National Authority (PNA) and to carry out all the operations necessary for the production and generation of electricity.

Gaza Power Generating Private Limited Company (GPGC/the subsidiary) has an exclusive right from PNA to provide capacity and generate electricity in Gaza for the benefit of entities owned or controlled by the PNA for 20 years following commercial operation of its power plant with the opportunity to continue for up to two additional consecutive five-year periods. Commercial operation started on March 15, 2004.

The Company is considered a subsidiary of Palestine Power Private Limited Company (PPP). PPP owns % 64.99 of the Company's share capital. The financial statements of the Company are consolidated with the financial statements of PPP.

The consolidated financial statements were authorized for issuance by the Company's board of directors on March 8, 2012.

### **2. Consolidated Financial Statements**

The consolidated financial statements comprise the financial statements of the Company and its wholly owned subsidiary, GPGC, as at December 31, 2011. GPGC was established in Gaza as a private shareholding limited company, with an authorized share capital of 6,000,000 shares of U.S. \$ 10 par value each.

#### **3.1 Basis of Preparation**

The consolidated financial statements of the Company and its subsidiary have been prepared in accordance with International Financial Reporting Standards as issued by International Accounting Standard Board (IASB) interpretations issued by International Financial Reporting Interpretations Committee (IFRIC).

The consolidated financial statements have been presented in U.S. Dollar, which is the functional currency of the Company

The consolidated financial statements have been prepared under the historical cost convention.

### 3.2 Basis of Consolidation

A subsidiary is a company over which the Company exercises control over the financial and operational policies.

The financial statements of the subsidiary, GPGC, are prepared for the same reporting year as the Company, using consistent accounting policies.

A subsidiary is fully consolidated from the date of acquisition, being the date on which the Company obtains control, and continues to be consolidated until the date that such control ceases.

All intra-company balances, transactions, income and expenses and profits and losses resulting from intra-company transactions that are recognized in assets, are eliminated in full.

### 3.3 Changes in Accounting Policies

The accounting policies adopted are consistent with those of the previous financial year except that the Company has adopted the following new and amended IFRS. Adoption of these standards and interpretations did not have any effect on the financial performance or position of the Company.

IAS 24 - Related Party Disclosures (Amendment)

IAS 32 - Financial Instruments: Presentation (Amendment)

The following standards have been issued but are not yet mandatory, and have not been adopted by the Company. These standards are those that the Company reasonably expects to have an impact on disclosures, financial position or performance when applied at a future date. The Company intends to adopt these standards when they become effective.

IAS 1 - Financial Statement Presentation - Presentation of Items of Other Comprehensive Income (Amendment) \*

IFRS 7 - Financial Instruments: Disclosures – (Amendment).

IFRS 9 - Financial Instruments: Classification and Measurement \*\*

IFRS 10 - Consolidated Financial Statements \*\*\*

IFRS 13 - Fair Value Measurement \*\*\*\*

\* The amendments to IAS 1 change the grouping of items presented in other comprehensive income. Items that could be reclassified (or 'recycled') to profit or loss at a future date would be presented separately from items that will never be reclassified. The amendment affects presentation only and has no impact on the Company's financial position or performance (effective for annual periods beginning on or after July 1, 2012).

\*\* IFRS 9 as issued reflects the first phase of the IASBs work on the replacement of IAS 39 and applies to classification and measurement of financial assets and financial liabilities as defined in IAS 39. The adoption of the first phase of IFRS 9 will have an effect on the classification and measurement of the Company's financial assets, but will potentially have no impact on classification and measurements of financial liabilities. The Company will quantify the effect in conjunction with the other phases, when issued, to present a comprehensive picture (effective for annual periods beginning on or after January 1, 2015).

\*\*\* IFRS 10 establishes a single control model that applies to all entities including special purpose entities. The changes will require management to exercise significant judgment to determine which entities are controlled, and therefore, are required to be consolidated by a parent, compared with the requirements that were in IAS 27 (effective for annual periods beginning on or after January 1, 2013).

\*\*\*\* IFRS 13 provides guidance on how to measure fair value under IFRS when fair value is required or permitted. The Company is currently assessing the impact that this standard will have on the financial position and performance (effective for annual periods beginning on or after January 1, 2013).

### **3.4 Estimates and Assumptions**

The preparation of the financial statements in conformity with IFRS requires the use of accounting estimates and assumptions. It also requires management to exercise its judgment in the process of applying the Company's accounting policies. The Company's management continually evaluates its estimates, assumptions and judgments based on available information and experience. As the use of estimates is inherent in financial reporting, actual results could differ from these estimates.

#### Useful lives of tangible and intangible assets

The Company's management reassesses the useful lives of tangible and intangible assets, and make adjustments if applicable, at each financial year end.

#### Impairment of accounts receivable

When the Company has objective evidence that it will not be able to collect certain debts, estimates, are used in determining the level of debts that the Company believes will not be collected.

The Company's management believes that the estimates and assumptions used are reasonable.

### **3.5 Summary of Significant Accounting Policies**

#### **Revenue recognition**

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Company and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognized:

#### Capacity charges

Capacity charge revenues from the use of the power plant are recognized during the period in which electricity is available according to the power purchase agreement signed with PENRA. This results in revenue recognition approximating the straight-line requirements of IAS (17) on leases.

The Company applies IFRIC (4) which relates to arrangements that do not take the legal form of a lease but convey the right to use an asset in return for a payment or a series of payments. An arrangement conveys the right to use the asset if the arrangement conveys to the purchaser (lessee) the right to control the use of the underlying asset. The right to control the use of the underlying asset is conveyed if any one of the following conditions is met:

- The purchaser has the ability or right to operate the asset or direct others to operate the asset in a manner it determines while obtaining or controlling more than an insignificant amount of the output or other utility of the asset.
- The purchaser has the ability or right to control physical access to the underlying asset while obtaining or controlling more than an insignificant amount of the output or other utility of the asset.
- Facts and circumstances indicate that it is remote that one or more parties other than the purchaser will take more than an insignificant amount of the output or other utility that will be produced or generated by the asset during the term of the arrangement, and the price that the purchaser will pay for the output is neither contractually fixed per unit of output nor equal to the current market price per unit of output as of the time of delivery of the output.

As the Palestinian Energy and Natural Resources Authority (PENRA) is the sole purchaser of the electricity generated from power plant at a price other than at market price and the price varies other than in response to market price changes, this variability is regarded by IFRIC (4) as capacity payments are being made for the right to use the power plant. Hence, such arrangement is accounted for in accordance with IAS (17) on leases. The power purchase agreement does not transfer substantially all the risks and rewards incidental to the Company's ownership of the power plant to PENRA. Therefore, the Company considered the arrangement of the power plant agreement as an operating lease and electrical capacity charges from the use of power plant to generate electricity as rental payment.

#### Interest revenues

Interest revenue is recognized as interest accrues using the effective interest method using the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset.

#### Government grants and assistance

A government's grant and assistance that becomes receivable as compensation for expenses or losses incurred for the purpose of giving immediate financial support to the entity with no future related costs shall be recognized as income for the period in which it becomes available.

Government grants and assistance are recognized where there is a reasonable assurance that the grant will be received and all attaching conditions will be complied with. When the grant relates to an expense item, it is recognized as income over the period necessary to match the grant on a systematic basis to the costs that it is intended to compensate.

A government's grant and assistance in the form of a transfer of a non-monetary asset, which is intended for use of the entity, is recognized at fair value of that asset. Fair value is the amount for which an asset could be exchanged between a knowledgeable willing buyer and a knowledgeable willing seller in an arm's length transactions.

### **Expense recognition**

Expenses are recognized when incurred in accordance with the accrual basis of accounting.

### **Finance costs**

Finance costs are recognized as an expense when incurred. Finance costs consists of interest using the effective interest method and other costs incurred in connection with borrowing of funds.

### **Property, plant and equipment**

Property, plant and equipment are stated at cost, net of accumulated depreciation and/or accumulated impairment losses, if any. Such cost includes the cost of replacing part of the property, plant and equipment and borrowing costs for long-term construction projects if the recognition criteria are met. All other repair and maintenance costs are recognized in the consolidated income statement as incurred. Depreciation is calculated on a straight line basis over the estimated useful lives of the assets as follows:

	<b>Useful lives (Years)</b>
Power plant	20
Building	20
Motor vehicles	5
Computers and printers	4
Office equipment	4
Furniture and fixture	5

Any item of property, plant, and equipment and any significant part initially recognized is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the consolidated income statement when the asset is derecognized.

The property, plant and equipment residual values, useful lives and methods of depreciation are reviewed at each financial year end and adjusted prospectively, if appropriate.

### **Intangible assets**

Intangible assets acquired through government grant and assistance are initially measured at fair value. Following initial recognition, intangible assets are carried net of any accumulated amortization and any accumulated impairment losses.

Intangible assets with finite lives are amortized over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset with a finite useful life is reviewed at least at each financial year

end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and treated as changes in accounting estimates. The amortization expense on intangible assets with finite lives is recognized in the consolidated income statement in the expense category consistent with the function of the intangible asset.

#### Right to use PENRA's transformers

Right to use PENRA's transformers is amortized using the straight-line method over a period equals the remaining useful life of the Power Plant at the time of acquiring the right to use these transformers being 17.5 years. Amortization expense is recognized in the consolidated income statement.

#### **Fair values**

For investments traded in an active market, fair value is determined by reference to quoted market bid prices at the close of business on the financial statements date.

The fair value of interest-bearing items is estimated based on discounted cash flows using interest rates for items with similar terms and risk characteristics.

For unquoted equity investments, fair value is determined by reference to the market value of a similar investment or is based on the expected discounted cash flows.

#### **Impairment and uncollectibility of financial assets**

An assessment is made at each financial statements date to determine whether there is objective evidence that a specific financial asset may be impaired. If such evidence exists, any impairment loss is recognized in the consolidated income statement. Impairment is determined as follows:

- For assets carried at fair value, impairment is the difference between cost and fair value, less any impairment loss previously recognized in the consolidated income statement;
- For assets carried at cost, impairment is the difference between carrying value and the present value of future cash flows discounted at the current market rate of return for a similar financial asset;
- For assets carried at amortized cost, impairment is the difference between carrying amount and the present value of future cash flows discounted at the original effective interest rate.

#### **Materials and inventories**

Materials and inventories are stated at the lower of cost using the weighted average method or net realizable value. Costs are those amounts incurred in bringing each item of materials and inventories to its present location and condition.

#### **Accounts receivable**

Accounts receivable are stated at original invoice amount less a provision for any impaired amounts. An estimate for impaired accounts receivable is made when collection of the full amount is no longer probable. Bad debts are written off when there is no possibility of recovery.

**Investment in an associate**

The Company's investment in its associates is accounted for using the equity method. An associate is an entity in which the Company has significant influence.

Under the equity method, the investment in the associates is carried in the statement of financial position at cost plus post acquisition changes in the Company's share of net assets of the associates.

The consolidated income statement reflects the share of the results of operations of the associate. Unrealized gains and losses resulting from transactions between the Company and the associate are eliminated to the extent of the interest in the associate.

The financial statements of the associate are prepared for the same reporting period as the Company. Where necessary, adjustments are made to bring the accounting policies in line with those of the Company.

**Cash and cash equivalents**

For the purpose of the statement of cash flows, cash and cash equivalents consist of cash on hand, bank balances, and short-term deposits with an original maturity of three months or less net of restricted bank deposits.

**Loans**

After initial recognition, interest bearing loans are subsequently measured at amortized cost using the effective interest rate method. Gains and losses are recognized in the consolidated income statement when the liabilities are derecognized as well as through the effective interest rate method (EIR) amortization process.

Amortized cost is calculated by taking into account any discount or premium on acquisition and fee or costs that are an integral part of the EIR. The EIR amortization is included in finance cost in the consolidated income statement.

**Accounts payable 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**

Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

**Provision for employees' indemnity**

Provision for employees' indemnity is calculated in accordance with the labor law prevailing in Palestine, and the Company's internal policies, based on one-month salary for each year of employment.

**Foreign currency**

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange ruling at the consolidated financial statements date. All differences are recognized to the consolidated income statement.

#### 4. Property, Plant and Equipment

	Power plant	Building	Motor vehicles	Computers and printers	Office equipment	Furniture and fixture	Total
	U.S. \$	U.S. \$	U.S. \$	U.S. \$	U.S. \$	U.S. \$	U.S. \$
<b>2011</b>							
<b>Cost</b>							
At January 1, 2011	135,440,605	1,464,904	440,392	287,117	138,197	195,170	137,966,385
Additions	-	-	-	18,582	-	1,990	20,572
At December 31, 2011	135,440,605	1,464,904	440,392	305,699	138,197	197,160	137,986,957
<b>Accumulated Depreciation</b>							
At January 1, 2011	52,936,035	411,402	257,273	252,467	127,775	184,873	54,169,825
Depreciation charges for the year	6,772,032	73,248	73,128	16,020	5,244	3,956	6,943,628
At December 31, 2011	59,708,067	484,650	330,401	268,487	133,019	188,829	61,113,453
<b>Net carrying amount</b>							
At December 31, 2011	75,732,538	980,254	109,991	37,212	5,178	8,331	76,873,504
	Power plant	Building	Motor vehicles	Computers and printers	Office equipment	Furniture and fixture	Total
	U.S. \$	U.S. \$	U.S. \$	U.S. \$	U.S. \$	U.S. \$	U.S. \$
<b>2010</b>							
<b>Cost</b>							
At January 1, 2010	135,440,605	1,464,904	440,392	271,470	138,197	188,194	137,943,762
Additions	-	-	-	15,647	-	6,976	22,623
At December 31, 2010	135,440,605	1,464,904	440,392	287,117	138,197	195,170	137,966,385
<b>Accumulated Depreciation</b>							
At January 1, 2010	46,164,020	338,154	184,120	228,844	122,539	173,326	47,211,003
Depreciation charges for the year	6,772,015	73,248	73,153	23,623	5,236	11,547	6,958,822
At December 31, 2010	52,936,035	411,402	257,273	252,467	127,775	184,873	54,169,825
<b>Net carrying amount</b>							
At December 31, 2010	82,504,570	1,053,502	183,119	34,650	10,422	10,297	83,796,560

Property, plant and equipment include U.S. \$ 610,586 and U.S. \$ 550,574 of fully depreciated assets as at December 31, 2011 and 2010, respectively, which are still used in the Company's operations.

## 5. Intangible Asset

	2011	2010
	U.S. \$	U.S. \$
Balance, beginning of the year	1,717,184	1,846,784
Amortization	(129,600)	(129,600)
Balance, end of year	1,587,584	1,717,184

Intangible asset represents the Company's right to use PENRA's four step-up transformers installed on October 1, 2006 for use by GPGC as part of the agreement signed on September 2, 2006 between GPGC and PENRA. According to the agreement, PENRA would rectify all damages within the power plant resulted from the Israeli air strike during June 2006 to restore the power supply from the power plant by agreeing to purchase and install six step-up transformers to replace GPGC's destroyed transformers. These transformers will be owned by PENRA; and GPGC will have the right to use such transformers and will be responsible for their operation and maintenance. The right to use the transformers was initially recognized at the fair value of the four step-up transformers already installed, amounted to U.S. \$ 2,267,984.

## 6. Prepayments

	2011	2010
	U.S. \$	U.S. \$
Land lease *	-	141,663
Legal fees **	-	164,912
	-	306,575

\* The land lease agreement was signed on November 25, 1999. The duration of the agreement is 30 years and may be further extended for an additional 10 years period. GPGC paid U.S. \$ 1,700,000 for the first 12 years of the lease period ended in 2011, after which the lease payments are fixed at U.S. \$ 147,000 annually for the remaining 18 years totaling U.S.\$ 2,646,000. Movement on prepaid land lease is as follows:

	2011	2010
	U.S. \$	U.S. \$
Balance, beginning of the year	141,663	283,330
Amortization of land lease for the year	(141,663)	(141,667)
Balance, end of year	-	141,663

\*\* During the year, GPGC amortized the last part of the legal fees incurred to obtain the long term loan. The fees were amortized over the loan original term of 11 years starting July 1, 2000. Amortization of legal fees is accounted for as finance costs. Movement during the year is as follows:

	2011	2010
	U.S. \$	U.S. \$
Balance, beginning of the year	164,912	494,736
Amortization for the year	(164,912)	(329,824)
Balance, end of year	-	164,912

## 7. Investment in an Associate

Company name	Country of Incorporation	Ownership %		2011	2010
		2011	2010	U.S.\$	U.S.\$
Palestine Power Generating Co.	Palestine	41	41	<u>1,008,805</u>	<u>112,577</u>

The Company worked with other investors on establishing Palestine Power Generating Company, public shareholding company (the associate) in the West Bank with an initial share capital of U.S. \$ 2,000,000 at a par value equal U.S.\$ 1 for each share with an intention to increase the capital to U.S. \$ 120,000,000 during the development of the power plant project which the associate intends to develop. The general assembly of the shareholders of the associate decided in an extraordinary meeting held on July 17, 2011 to increase the share capital to 10 million shares, fully subscribe to the shareholders. The Company's investment in associate represents the amounts paid by the Company in share of net assets of the associate reduced by the Company's share of the associate results of operation.

Company's share of the associate's assets and liabilities is as follows:

	2011	2010
	U.S. \$	U.S. \$
Non-current assets	<u>692,651</u>	<u>173,812</u>
Current assets	<u>971,451</u>	<u>167,172</u>
Non-current liabilities	<u>9,664</u>	<u>5,481</u>
Current liabilities	<u>93,608</u>	<u>286,934</u>

Company's share of the associate's revenues and results of operations for the year is as follows:

	2011	2010
	U.S. \$	U.S. \$
Revenue	<u>-</u>	<u>-</u>
Results of operations	<u>(218,772)</u>	<u>(92,423)</u>

## 8. Materials and Inventories

	2011	2010
	U.S. \$	U.S. \$
Spare parts	5,545,964	5,217,648
Consumables	255,944	212,000
Goods in transit	771,092	819,432
Others	19,855	17,468
	<u>6,592,855</u>	<u>6,266,548</u>

## 9. Accounts Receivable

	2011	2010
	U.S. \$	U.S. \$
Accounts receivable from capacity charges	26,809,172	25,845,791
Force majeure government assistance receivable (note 20)	-	3,548,533
	26,809,172	29,394,324
Impairment of accounts receivable	(6,756,132)	(6,756,132)
	<u>20,053,040</u>	<u>22,638,192</u>

Impaired account receivable amounted to U.S. \$ 16,814,387 as of December 31, 2011 and U.S. \$ 12,605,449 as of December 31, 2010.

The aging analysis of the unimpaired accounts receivable as at December 31, 2011 and 2010 is as follows:

		Past due but not impaired			
	Neither past due nor impaired	Less than 30 days	30-60 days	61-120 days	
	Total U.S.\$	U.S.\$	U.S.\$	U.S.\$	U.S.\$
<b>2011</b>	9,994,785	2,576,383	2,029,281	2,557,685	2,831,436
<b>2010</b>	16,788,875	2,555,510	4,165,562	5,066,403	5,001,400

Unimpaired receivables are expected, on the basis of past experience, to be fully recoverable. All GPGC capacity charges revenue from the use of power plant is generated from one customer, PENRA. According to the power purchase agreement, PENRA is required to provide GPGC with a letter of credit of U.S. \$ 20,000,000 from a qualified bank as defined in the agreement. To the date of these consolidated financial statements, PENRA has not provided GPGC with the letter of credit, therefore, accounts receivable are unsecured.

## 10. Other Current Assets

	2011	2010
	U.S. \$	U.S. \$
Due from PENRA *	1,133,992	1,133,992
Value Added Tax receivable	134,841	162,015
Due from shareholders	1,197,594	572,478
Due from an associate	252,250	61,737
Prepaid insurance	414,480	386,372
Advances to suppliers	1,517,188	1,453,147
Others	21,111	49,322
	<u>4,671,456</u>	<u>3,819,063</u>

\* The amount represents the fair value of the two remaining transformers that PENRA is committed to supply and install in accordance with the agreement signed between GPGC and PENRA on September 2, 2006 (note 5). PENRA has made a commitment to supply and install the two transformers as soon as the situation in Gaza permits.

## 11. Cash and Bank Accounts

	<u>2011</u>	<u>2010</u>
	<u>U.S. \$</u>	<u>U.S. \$</u>
Cash on hand	6,836	9,000
Current accounts at banks in U.S. \$	6,932,832	5,884,895
	<u>6,939,668</u>	<u>5,893,895</u>

## 12. Paid-in Share Capital

	<u>2011</u>	<u>2010</u>
	<u>U.S. \$</u>	<u>U.S. \$</u>
Authorized share capital	60,000,000	60,000,000
Subscribed share capital	60,000,000	60,000,000
Paid-in share capital	60,000,000	60,000,000

The share capital of the Company comprises 60,000,000 ordinary shares at par value equals U.S. \$ 1 for each share.

## 13. Statutory Reserve

The amount represents cumulative transfers of 10% of profits to statutory reserve in accordance with the Companies' Law.

## 14. Long Term Loan

On June 26, 2000, GPGC signed an agreement with Arab Bank P.L.C. for a long term loan of U.S. \$ 90,000,000. On November 16, 2003, GPGC signed a restatement and amendment agreement of the long term loan with the Arab Bank. According to the agreement, the long term loan will be repayable over 19 semi-annual installments the first of which started on December 31, 2004 and the last installment becomes due on December 31, 2013. These installments are based on predetermined percentage of the loan amount. It has also been agreed that interest rate on the long term loan is six month LIBOR plus 2.25%. Interest rate was further reduced to six month LIBOR plus 2% effective December 31, 2007.

During 2011, GPGC and Arab Bank agreed to transfer an amount of U.S. \$ 30 million that was transferred to the Company from Palestinian Authority for the settlement of PENRA's accounts receivable to Arab Bank to be used to settle the loan's passed due installments, interests, and commissions and prepay outstanding loan installments in advance. Further, the parties agreed to settle the remaining balance of the loan amounted to U.S.\$ 6,973,393 over two equal installments the first of which payable on September 30, 2011 and the second on December 31, 2011.

Subsequent to the financial statements date, the parties agreed to reschedule the loan's balance of U.S.\$ 6,973,393 over two installments the first of which amounting to U.S.\$ 2,257,000 plus related interest will payable on June 30, 2013 and the second installment amounting to U.S.\$ 4,716,393 plus related interest payable on December 31, 2013.

As a collateral for the loan, Arab Bank has a security pledge over all GPGC assets and all of GPGC shares owned by the Company.

The main financial covenants of the loan agreement include keeping certain financial ratios before any distribution of dividends is approved, maintaining current corporate existence of the Company, investing only in assets allowed by the loan agreement and not incurring indebtedness unless previously approved by Arab Bank.

After obtain Arab Bank consent, GPGC signed an agreement on September 28, 2011 with one of local banks to obtain a long term loan in the amount of U.S. \$ 11,000,000. The loan is repayable over 10 equal semi-annual installments the first which will be due on April 1, 2013 and last installment will be due on October 1, 2017. The loan is subject to an annual interest rate of six month LIBOR plus 2% with minimum rate of %5 and maximum of 7% and an annual commission at a rate of 0.5%. The Company agreed to share all collaterals made available to the Arab Bank against the Arab Bank loan, referred to above, with the local bank.

Payment schedule of the loans is as follows:

	<u>U.S. \$</u>
2012	-
2013	9,173,393
2014	2,200,000
2015	2,200,000
2016	2,200,000
2017	<u>2,200,000</u>
	<u><u>17,973,393</u></u>

## 15. Provision for Employees' Indemnity

Movement on the provision for employees' end of service indemnity during the year was as follows:

	<u>2011</u>	<u>2010</u>
	<u>U.S. \$</u>	<u>U.S. \$</u>
Balance, beginning of the year	1,795,186	1,407,972
Additions	246,222	413,058
Payments	<u>(121,050)</u>	<u>(25,844)</u>
Balance, end of year	<u><u>1,920,358</u></u>	<u><u>1,795,186</u></u>

## 16. Credit Facilities

On January 24, 2011, GPGC signed agreement with Arab Bank to obtain credit facilities in the form of overdraft with ceiling of U.S. \$ 3,000,000 subject to annual interest rate of LIBOR for six months plus 2.75% and annual commission of rate 0.5%. The utilized balance of the overdraft is to be settled after one year from the agreement signing date or any date the parties subsequently agree thereon. The parties further agreed during the year to increase the ceiling of the credit facilities by U.S. \$ 2,000,000 subject to interest rate of LIBOR for one month plus 2.75% and commission rate of 3.5% and agreed to settle the additional granted credit facilities no later than July 31, 2011.

Subsequent to the financial statements date, the Arab Bank agreed to extend the credit facilities, amounting to U.S.\$ 3,000,000 repayment due date to January 31, 2013 and further agreed to extend the due date of the utilized balance of the additional credit facilities to a date no later than August 1, 2012.

Repayment schedule of the credit facilities is as follows:

	U.S. \$
Credit facilities mature in 2012	1,501,000
Credit facilities mature in 2013	2,849,000
	<u>4,350,000</u>

## 17. Other Current Liabilities

	2011	2010
	U.S. \$	U.S. \$
Accrued finance cost	193,551	572,394
Provision for maintenance expenses	4,772,021	1,798,623
Dividends payable	6,465,079	2,020,247
Due to Consolidated Contractors Company	236,337	55,568
Accrued board of directors remuneration	164,500	-
Payroll income tax *	494,942	503,225
Accrued expenses	1,601,826	95,192
Provision for employees' vacations	212,488	219,126
Other provisions	1,199,606	1,177,256
	<u>15,340,350</u>	<u>6,441,631</u>

\* The Company did not withhold income tax on employees salaries based on the presidential decree issued in June 2007 exempting all tax payers of southern governorates (Gaza Strip) from taxes.

## 18. Capacity Charges

The amount represents revenues from capacity charges invoices issued by GPGC for the use of power plant to generate electric capacity for the benefit of PENRA according to the power purchase agreement, which is considered an operating lease under IFRIC (4) as further explained in accounting policies note (3.5).

Capacity charges are materially straight-line over the life of the plant which results in revenue recognition approximating the straight-line requirements of IAS (17) on leases. According to the agreement, PENRA shall pay for all the electric capacity available from the use of GPGC's power plant, regardless of the extent to which PENRA can absorb that capacity, for a predetermined price set out in the power purchase agreement for each operating year. In addition, PENRA shall, at all times, supply and deliver all the fuel required to generate the power needed.

## 19. Operating Expenses

	2011	2010
	U.S. \$	U.S. \$
Salaries and wages	4,364,483	4,149,777
Employees' indemnity	246,222	413,058
Board of directors remuneration	164,500	164,500
Employees' insurance	127,268	125,186
Development and technical advisory services	820,000	2,634,845
Travel and transportation	492,324	488,991
Power plant insurance	796,756	799,009
Power plant operation and maintenance	5,899,048	3,946,896
Depreciation of property, plant and equipment	6,943,628	6,958,822
Amortization of intangible asset	129,600	129,600
Amortization of land lease	141,663	141,667
Professional and consultancy fees	286,156	390,499
Telephone and fax	96,274	101,918
Legal fees	20,534	20,520
Palestine Exchange listing fee	24,224	24,874
Office supplies	53,536	84,747
Advertisements	13,602	281,185
Security service costs	577,169	622,229
Miscellaneous	162,997	479,406
	<u>21,359,984</u>	<u>21,957,729</u>

## 20. Force Majeure Government Assistance

The item represents financial assistance provided from PENRA to GPGC to cover force majeure events that caused GPGC to incur maintenance costs as results of the political and security situation in Gaza. GPGC received U.S. \$ 3,128,036 during the 2010 and an amount of U.S. \$ 3,548,533 during 2011.

## 21. Basic and Diluted Earnings Per Share

	2011	2010
	U.S. \$	U.S. \$
Profit for the year	<u>8,374,034</u>	<u>6,782,383</u>
	Shares	Shares
Weighted average of subscribed share capital during the year	<u>60,000,000</u>	<u>60,000,000</u>
	U.S. \$	U.S. \$
Basic and diluted earnings per share	<u>0.14</u>	<u>0.11</u>

## 22. Dividends

The Company's general assembly, in its meeting held on April 27, 2011, approved the proposed dividends distribution by the Company's board of directors of U.S. \$ 6,000,000 for the year 2010, the equivalent of 10% of paid-in share capital.

The Company's general assembly, in its meeting held on April 25, 2010, approved the proposed dividends distribution by the Company's board of directors of U.S. \$ 6,000,000 for the year 2009, the equivalent of 10% of paid-in share capital.

## 23. Related Party Transactions

Related parties represent associated companies, major shareholders, directors and key management personnel of the Company and GPGC, and companies of which they are principal owners. Pricing policies and terms of these transactions are approved by the Company's board of directors. Balances with related parties included in the consolidated statement of financial position are as follows:

	Nature of relation	2011 U.S. \$	2010 U.S. \$
Cash at Arab Bank	Major shareholder	2,609,500	5,884,895
Due from shareholders	Major shareholders	1,197,594	572,478
Due from an associate	Associate	252,250	61,737
Arab Bank long term loan	Major shareholder	6,973,393	40,545,000
Credit facilities	Major shareholder	4,350,000	-
Accrued interest loan	Major shareholder	193,551	572,394
Due to Consolidated Contractors Company	Major shareholder	236,337	55,568
Accrued board of directors remuneration	Board of directors	164,500	-

The consolidated income statement includes the following transactions with related parties:

	Nature of relation	2011 U.S. \$	2010 U.S. \$
Arab Bank finance cost	Major shareholder	574,660	1,492,541
Development and technical advisory services charged by United Engineering Services S.A	Sister company	-	2,284,845
Consulting and service fee charged by Consolidated Contractors Company	Major shareholder	299,000	564,000

Compensation of key management personnel:

Salaries and wages	497,348	613,835
Employees' end of service benefits	31,506	39,318
Board of directors remuneration	164,500	164,500

## 24. Income Tax

The PNA has agreed to exempt GPGC and its shareholders (with respect to dividends and earnings from GPGC), for the term of the agreement of 20 years including any extensions thereof, from all Palestinian taxes.

## 25. Commitments and Contingencies

Commitments and contingencies represent the following:

	2011	2010
	U.S. \$	U.S. \$
Long term maintenance service agreement *	10,132,088	12,200,969
Land lease agreement (note 6)	2,646,000	2,646,000
Unpaid share of investment in an associate	2,780,000	615,000
Development and technical consulting agreement	1,830,000	-
	<u>17,388,088</u>	<u>15,461,969</u>

\* The long term maintenance service agreement represents the difference between the contract gross amount of Swedish Krona (SEK) 179,000,000 and the executed portion of the contract at the financial statements date. The unexecuted portion of the contract amounted to SEK 70,047,175 and SEK 86,266,813 as of December 31, 2011 and 2010, respectively.

Future minimum capacity charge expected to be receivable under the power purchase agreement for the use of power plant in effect as of December 31, 2011 and 2010 were as follows:

	2011	2010
	U.S. \$	U.S. \$
Within one year	30,167,928	29,890,896
After one year and up to five years	123,609,312	122,416,726
More than five years	237,547,392	268,907,906
	<u>391,324,632</u>	<u>421,215,528</u>

## 26. Fair Values of Financial Instruments

Financial instruments comprise of financial assets and financial liabilities. Financial assets consist of cash and bank accounts, accounts receivable and some other current assets. Financial liabilities consist of long term loan and some other current liabilities.

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

## 27. Risk Management

The Company's principal financial liabilities comprise long term loan, credit facilities and some other current liabilities. The main purpose of these financial liabilities is to raise finance for the Company's operations. The Company has various financial assets such as accounts receivable, cash and bank accounts, and some other current assets which arise directly from the Company's operations.

The main risks arising from the Company's financial instruments are interest rate risk, credit risk, liquidity risk, and foreign currency risk. The Company's Board of Directors reviews and approves policies for managing these risks which are summarized below.

## Interest rate risk

The following table demonstrates the sensitivity of the consolidated income statement to reasonably possible changes in interest rates as of December 31, 2011, with all other variables held constant.

The sensitivity of the consolidated income statement is the effect of the assumed changes in interest rates on the Company's profit for one year, based on the floating rate of financial assets and financial liabilities at December 31, 2011 and 2010. There is no direct impact on the Company's equity. The effect of decrease in interest rate is expected to be equal and opposite to the effect of increases shown below:

	Increase in interest rate Basis points	Effect on profit for the year U.S. \$
<b><u>2011</u></b>		
U.S. Dollar	+10	(22,323)
<b><u>2010</u></b>		
U.S. Dollar	+10	(40,545)

## Credit risk

The Company is currently exposed to credit risk as all the revenues of its subsidiary from the use of the power plant to generate electric capacity is generated from one customer, PENRA. PENRA has not provided the Company's subsidiary with required letter of credit of U.S. \$ 20,000,000 as required by the power purchase agreement.

With respect to credit risk arising from the other financial assets, the Company's exposure to credit risk arises from the possibility of default of the counterparty, with a maximum exposure equal to the carrying amount of these other financial assets.

## Liquidity risk

The Company and of its subsidiary limit their liquidity risk by ensuring bank facilities are available and by maintaining adequate cash balances to meet their current obligations and to finance its operating activities and by following up on the collection of accounts receivable from PENRA. The table below summarizes the maturity profile of the Company's financial liabilities at December 31, 2011 and 2010 based on contractual undiscounted payments.

	Less than 3 Months U.S.\$	3 to 12 months U.S.\$	More than 1 year up to 5 years U.S.\$	Total U.S.\$
<b><u>December 31, 2011</u></b>				
Long term loans	-	-	20,358,547	20,358,547
Credit facilities	-	1,673,512	2,863,376	4,536,888
Other current liabilities	711,740	6,553,319	-	7,265,059
	<u>711,740</u>	<u>8,226,831</u>	<u>23,221,923</u>	<u>32,160,494</u>
	Less than 3 Months U.S.\$	3 to 12 months U.S.\$	More than 1 year up to 5 years U.S.\$	Total U.S.\$
<b><u>December 31, 2010</u></b>				
Long term loan	6,003,000	13,649,632	22,938,373	42,591,005
Other current liabilities	640,108	2,280,549	-	2,920,657
	<u>6,643,108</u>	<u>15,930,181</u>	<u>22,938,373</u>	<u>45,511,662</u>

### Foreign currency risk

The table below indicates the Company's foreign currency exposure, as a result of its monetary assets and liabilities. The analysis calculates the effect of a reasonably possible movement of the U.S. \$ currency rate against foreign currencies, with all other variables held constant, on the consolidated income statement. The effect of decrease in foreign currency exchange rate is expected to be equal and opposite to the effect of increases shown below:

	Increase in EURO rate to U.S.\$ %	Effect on profit for the year U.S.\$	Increase in ILS rate to U.S.\$ %	Effect on profit for the year U.S.\$	Increase in SEK rate to U.S.\$ %	Effect on profit for the year U.S.\$
<b>2011</b>						
U.S.\$	+10	(24,860)	+10	(14,073)	+10	29,257
<b>2010</b>						
U.S.\$	+10	(28,601)	+10	(19,352)	+10	78,959

### Capital management

The primary objective of the Company's capital management is to ensure that it maintains healthy capital ratios in order to support its business and maximize shareholder value.

The Company manages its capital structure and makes adjustments to it in light of changes in business conditions. No changes were made in the objectives, policies or processes during the years ended December 31, 2011 and 2010. Capital comprises paid-in share capital, statutory reserve and retained earnings, and is measured at U.S. \$ 78,142,811 and U.S. \$ 75,768,777 as at December 31, 2011 and 2010, respectively.

## 28. Concentration of Risk in Geographic Area

The Company and of its subsidiary are carrying out all of their activities in Gaza. Assets, which mainly comprise property, plant and equipment, are located in Gaza. The political and economical situation in the area increases the risk of carrying out business and could adversely affect their performance and impacts the recoverability of their assets from operation.