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AUDITOR'S REPORT TO THE SHAREHOLDERS OF ISLAMIC BANK OF YEMEN FOR FINANCE AND INVESTMENT SANA'A, REPUBLIC OF YEMEN

We have audited the accompanying financial statements of Islamic Bank of Yemen for Finance and Investment represented in the balance sheet as of December 31, 2005, the related statements of income, cash flows, changes in shareholders' equity and statement of sources and uses of Qard Hasan, for the year then ended. These financial statements and the bank's undertaking to operate in accordance with Islamic Sharia' rules and principles are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with International Standards on Auditing and the Auditing Standards for Islamic Financial Institutions and the requirements of relevant Yemeni laws and regulations. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We have obtained from management the information and clarifications that we deemed necessary for our audit and we believe that our audit provides a reasonable basis for our opinion.

In application of Central Bank of Yemen circulars no. 6 of 1996 and no. 5 of 1998 concerning the classification of assets and contingent liabilities, and making the required provisions, and their impact on the financial statements, there is a shortfall in the provision amount, as explained in note (10) to the financial statements.

Except for the effects on the financial statements of the matter referred to in the preceding paragraph, in our opinion, the accompanying financial statements are prepared, in all material respects, in accordance with the accounting requirements of Central Bank of Yemen, Accounting Standards for Islamic Financial Institutions and applicable local laws and regulations.

The bank keeps proper books of account, and the accompanying financial statements are in agreement with those books.


M. Zohdi Mejanni
Associated Accountant



Sana'a, April 26, 2006

**ISLAMIC BANK OF YEMEN FOR FINANCE AND INVESTMENT
SANA'A, REPUBLIC OF YEMEN**

**BALANCE SHEET
AS AT DECEMBER 31, 2005**

	<u>Note</u>	<u>2005 YR 000's</u>	<u>2004 YR 000s</u>
Assets			
Cash on hand & reserve balances with Central Bank	8	3,666,310	3,246,953
Due from banks and financial institutions	9	951,412	2,284,846
Financing Murabaha transactions (net)	3-3,10	6,836,919	7,097,909
Investments in Musharaka contracts (net)	3-4,12	364,422	558,063
Investment in Mudaraba Contracts (net)	3-4,14	515,155	699,076
Available for sale investments	3-5,16	136,852	12,230
Investment property	3-6,17	276,161	-
Restricted investments	3-7	771,508	1,182,637
Qard Hasan (net)		17,773	9,607
Debit balances & other assets (Net)	18	5,355,398	5,367,039
Property and equipment (Net)	3-11,20	287,567	313,490
Total assets		<u>19,179,477</u>	<u>20,771,850</u>
Liabilities, investment accounts and shareholders' equity			
Liabilities			
Current accounts and other deposits	21	5,176,353	8,513,412
Due to banks and financial institutions	22	2,212,370	112,960
Credit balances & other liabilities	23	1,070,342	1,270,867
Other provisions	25	142,009	159,395
Dividends payable		-	1,450
Total liabilities		<u>8,601,074</u>	<u>10,058,084</u>
Unrestricted investment and saving accounts' holders	26	<u>7,689,019</u>	<u>7,917,550</u>
Restricted investment accounts		<u>771,508</u>	<u>1,182,637</u>
Total liabilities, unrestricted and restricted accounts		<u>17,061,601</u>	<u>19,158,271</u>
Shareholders' equity			
Paid up capital	27	1,974,297	1,250,000
Reserves	28	142,607	351,607
Retained earnings		972	11,972
Total shareholders' equity		<u>2,117,876</u>	<u>1,613,579</u>
Total liabilities, investment accounts and shareholders' equity		<u>19,179,477</u>	<u>20,771,850</u>
Contingent liabilities and commitments	3-9,30	<u>12,900,773</u>	<u>16,834,191</u>

(The accompanying notes from 1 to 45 form part of these financial statements)

Chairman
General Manager
Financial Manager



Auditor's report attached.

M. Zohdi Mejanni
(KPMG Mejanni, Hazem Hassan & Co.)



**ISLAMIC BANK OF YEMEN FOR FINANCE AND INVESTMENT
SANA'A, REPUBLIC OF YEMEN**

**STATEMENT OF INCOME
FOR THE YEAR ENDED DECEMBER 31, 2005**

	<u>Note</u>	<u>2005 YR 000's</u>	<u>2004 YR 000's</u>
Revenues of Murabaha contracts financing	31	696,531	557,587
Revenues of other joint investments	32	<u>75,908</u>	<u>101,230</u>
		772,439	658,817
Less:			
Return of unrestricted investment accounts		(643,000)	(502,000)
The bank's share in the return on Murabaha and joint investments		129,439	156,817
The bank's share in restricted investments income		44,366	36,923
Commissions & fees income on banking services	33	619,449	609,870
Gain of foreign currency transactions	34	261,750	157,484
Losses of financial investments evaluation		(926)	-
Other operating income	35	<u>19,877</u>	<u>7,615</u>
Operating profit		1,073,955	968,709
Less:			
Provisions	36	(413,902)	(390,508)
Commissions & fees expenses on banking services		(16,300)	(6,738)
General & administration expenses and depreciation	37	<u>(643,753)</u>	<u>(550,018)</u>
Net profit before tax		-	21,445
Income tax for the year		<u>-</u>	<u>(6,998)</u>
Net profit		<u>-</u>	<u>14,447</u>
Earnings per share (YR)	38	<u>-</u>	<u>10.40</u>

(The accompanying notes from 1 to 45 form part of these financial statements)



Chairman

General Manager

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ISLAMIC BANK OF YEMEN FOR FINANCE AND INVESTMENT
SANA'A, REPUBLIC OF YEMEN

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2005

	<u>Note</u>	<u>2005</u> <u>YR 000s</u>	<u>2004</u> <u>YR 000s</u>
<u>Cash flows from operating activities:</u>			
Net result before tax		-	14,447
Adjustments to reconcile net result / profit to cash flows from operating activities			
Depreciation		69,267	67,580
Provisions	36	413,902	390,508
Provision used		(18,983)	(10,471)
Paid income taxes		(6,998)	(46,500)
(Gain) loss on sale of property and equipment		(421)	247
Return of unrestricted investment and saving accounts		<u>643,000</u>	<u>502,000</u>
<u>Operating profit before changes in assets & liabilities related to operating activities</u>		1,099,767	917,811
(Increase) in reserve balances with CBY		(574,341)	(446,387)
(Increase) decrease in Qard Hasan		(10,636)	1,745
Decrease (increase) in debit balances and other assets		15,770	(2,386,627)
Increase in credit balances and other liabilities		<u>13,182</u>	<u>284,415</u>
Net cash flows provided by (used in) operating activities (1)		<u>543,742</u>	<u>(1,629,043)</u>
<u>Cash flows from investing activities:</u>			
(Increase) decrease in available for sale investments		(124,622)	922
(Increase) in Murabaha financing contracts		(363,496)	(136,871)
Decrease in Musharaka contracts		195,597	11,423
Decrease (increase) in Mudaraha contracts		185,778	(485,860)
(Increase) in investment property		(276,161)	-
Decrease (increase) in restricted investments		411,129	(156,134)
Payments to purchase property and equipment		(42,973)	(74,567)
Proceeds from sale of property and equipment		<u>50</u>	<u>33,997</u>
Net cash flows (used in) investing activities (2)		<u>(14,698)</u>	<u>(807,090)</u>
<u>Cash flows from financing activities:</u>			
Capital cash increase		504,297	-
Increase in due to banks and financial institutions		2,099,410	46,038
(Decrease) increase in unrestricted investment and saving accounts		(871,531)	713,580
(Decrease) increase in current accounts and other deposits		(3,337,059)	1,516,576
(Decrease) increase in unrestricted investments		(411,129)	156,134
Dividends paid		(1,450)	(168,582)
Net cash flows (used in) provided by financing activities (3)		<u>(2,017,462)</u>	<u>2,263,746</u>
Net change in cash and cash equivalent (1+2+3)		(1,488,418)	(172,387)
Cash and cash equivalent at beginning of the year		<u>2,952,023</u>	<u>3,124,410</u>
Cash and cash equivalent at end of the year		<u>1,463,605</u>	<u>2,952,023</u>
<u>Cash and cash equivalent consist of:</u>			
Cash on hand & current accounts with CBY		661,411	1,413,794
Due from banks and financial institutions		<u>802,194</u>	<u>1,538,229</u>
Total		<u>1,463,605</u>	<u>2,952,023</u>

(The accompanying notes from 1 to 45 form part of these financial statements)

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ISLAMIC BANK OF YEMEN FOR FINANCE AND INVESTMENT
SANA'A, REPUBLIC OF YEMEN

STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
FOR THE YEAR ENDED DECEMBER 31, 2005

	<u>Paid up Capital YR 000s</u>	<u>Statutory Reserve YR 000s</u>	<u>General Reserve YR 000s</u>	<u>Retained Earnings YR 000s</u>	<u>Total YR 000s</u>
Year 2005					
Balance at beginning of the year	1,250,000	142,607	209,000	11,972	1,613,579
Capital increase from reserves	220,000	-	(209,000)	(11,000)	-
Capital increase - cash	<u>504,297</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>504,297</u>
Balance at end of the year	<u>1,974,297</u>	<u>142,607</u>	<u>-</u>	<u>972</u>	<u>2,117,876</u>
Year 2004					
Balance at beginning of the year	1,250,000	140,657	209,000	925	1,600,582
Net profit of the year	-	-	-	14,447	14,447
Transfer to reserves	-	1,950	-	(1,950)	-
Board of Directors remuneration	<u>-</u>	<u>-</u>	<u>-</u>	<u>(1,450)</u>	<u>(1,450)</u>
Balance at end of the year	<u>1,250,000</u>	<u>142,607</u>	<u>209,000</u>	<u>11,972</u>	<u>1,613,579</u>

(The accompanying notes from 1 to 45 form part of these financial statements)

Chairman

 General Manager

 Financial Manager




Auditor's report attached.


 M. Zohdi Mejanni
 (KPMG Mejanni, Hazem Hassan & Co.)



**ISLAMIC BANK OF YEMEN FOR FINANCE AND INVESTMENT
SANA'A, REPUBLIC OF YEMEN**

**STATEMENT OF SOURCES AND USES OF QARD HASAN
FOR THE YEAR ENDED DECEMBER 31, 2005**

	<u>2005</u> <u>YR 000s</u>	<u>2004</u> <u>YR 000s</u>
<u>Opening balance, represented in:</u>		
Outstanding loans	10,533	12,264
<u>Add: Sources of Qard Hasan</u>		
Transfer from customers' current accounts	17,114	-
<u>Less: Uses of Qard Hasan</u>		
Payment to customers' current accounts	(6,478)	(1,731)
<u>Ending balance, represented in:</u>		
Outstanding loans	21,169	10,533
Less: provision of Qard Hasan	(3,396)	(926)
	<u>17,773</u>	<u>9,607</u>

(The accompanying notes from 1 to 45 form part of these financial statements)

Chairman

General Manager

Financial Manager



Auditor's report attached.

M. Zohdi Mejanni
(KPMG Mejanni, Hazem Hassan & Co.)



**ISLAMIC BANK OF YEMEN FOR FINANCE AND INVESTMENT
SANA'A, REPUBLIC OF YEMEN**

**NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2005**

1. BACKGROUND INFORMATION

The Islamic Bank of Yemen for Finance and Investment, a Yemeni Joint – Stock Company (Y.S.C.) was incorporated pursuant to the Minister of Trade and Supply Decree No. 137 of 1995. The bank carries out its banking activity in the Republic of Yemen through its Head office and 5 branches in Sana'a, Hodeidah, Taiz and Aden (Crater and Sheikh Othman).

The Bank was established for the purpose of covering the social and economic needs in investment, finance and banking services in conformity with the principles of the Islamic Shari'a. The Bank commenced operations on June 8, 1996. In accordance with Article No. (26) of Law No. (21) for 1996 regarding Islamic Banks, the Bank is entitled to all privileges and exemptions as stated in the Investment Law.

2. PREPARATION BASIS OF THE FINANCIAL STATEMENTS

The financial statements are prepared under the historical cost principle in accordance with Accounting Standards for Islamic Financial Institutions, local prevailing laws and regulations and in the light of rules and instructions issued by Central Bank of Yemen.

3. SIGNIFICANT ACCOUNTING POLICIES

3-1. Translation of foreign currencies

The bank maintains its accounting records in Yemeni Rial. Transactions in other currencies are recorded during the financial year at the prevailing exchange rates at the date of transaction. Balances of monetary assets and liabilities in other currencies at the end of the financial year are translated at the prevailing exchange rates on that date. Gains or losses resulting from translation are taken to the statement of income.

3-2. Revenue recognition

A. Murabaha

- Profits on Murabaha contracts are recorded on the accrual basis as all profits at the completion of Murabaha contract are recorded as deferred revenues and taken to the statement of income, based on the finance percentage, using the straight line method over the term of contract.
- In order to comply with the requirements of CBY, the bank does not accrue the revenues relating to non-performing Murabaha contracts.

**ISLAMIC BANK OF YEMEN FOR FINANCE AND INVESTMENT
SANA'A, REPUBLIC OF YEMEN**

**NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED DECEMBER 31, 2005**

B. Mudaraba and Musharaka

- Profits on Mudaraba and Musharaka contracts, which initiate and terminate during the financial year, are recorded in the statement of income at the liquidation date of the contract.
- Profits on Mudaraba and Musharaka contracts, which last for more than one financial year, are recorded, based on cash profits distributed on these transactions during the year.

C. Available for sale investments

Income from available for sale investments is recognized when its related dividends are distributed.

3-3. *Valuation of Murabaha financing transactions*

- Debts related to Murabaha financing transactions whether short or long term are recorded at cost in addition to agreed-upon profits in Murabaha contracts. In order to comply with the requirements of CBY, a provision is provided for specific Murabaha contracts and contingent liabilities, in addition to a percentage for general risk calculated on the total of other Murabaha contracts and contingent liabilities after deducting balances secured by deposits and banks' guarantees issued by worthy banks. The provision is determined based on periodical comprehensive reviews of the portfolio and contingent liabilities and made in accordance with the following minimum rates:

<u>Performing debts and special attention</u>	1%
<u>Non-performing debts:</u>	
Substandard debts	15%
Doubtful debts	45%
Bad debts	100%

- Debts relating to financing Murabaha transactions are written off if procedures taken toward their collection prove useless, or if directed by CBY examiners upon review of the portfolio. Proceeds from debts previously written off in prior years are credited to the provision.

**ISLAMIC BANK OF YEMEN FOR FINANCE AND INVESTMENT
SANA'A, REPUBLIC OF YEMEN**

**NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED DECEMBER 31, 2005**

- Debts relating to financing Murabaha transactions whether short or long term are presented on the balance sheet net provision, (non-performing debts provision and general risk provision on performing debts), deferred revenues and suspense revenues.

3-4. Valuation of Mudaraba and Musharaka contracts

- Investments in cash Mudaraba and Musharaka contracts are recorded on the basis of the amount paid to the capital of Mudaraba or Musharaka, while investments in inkind Mudaraba and Musharaka contracts are recorded based on the agreed-upon value between the bank and the customer or partner. Any differences between this value and the book value are recorded as profits or losses in the income statement.

In order to comply with the requirements of CBY, a provision is provided for specific Mudaraba and Musharaka contracts which recognized losses, in addition to a percentage for general risk calculated on the total of other Mudaraba and Musharaka contracts after deducting balances secured by the deposits and bank's guarantees issued by worthy banks.

The provision is determined based on periodical comprehensive reviews of the portfolio and made in accordance with the following rates:

<u>Performing debts and special attention</u>	1%
<u>Non-performing debts:</u>	
Substandards debts	15%
Doubtful debts	45%
Bad debts	100%

- At the end of each financial year, Mudaraba and Musharaka capitals are reduced by losses incurred. These losses are charged to the income statement.
- Investments in Mudaraba and Musharaka contracts are presented on the balance sheet at carrying value (cost less recognized losses and related provisions).

3.5. Valuation of available for sale investments

Available for sale investments are recorded at acquisition cost. At the financial statements date, they are individually valued at fair value. Valuation differences are charged to the statement of income in accordance with Central Bank of Yemen instructions.

In case that reliable estimate of the fair value of these investments can not be obtained, due to lack of quoted market prices, they are recorded at cost.

**ISLAMIC BANK OF YEMEN FOR FINANCE AND INVESTMENT
SANA'A, REPUBLIC OF YEMEN**

**NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED DECEMBER 31, 2005**

3.6. Valuation of investment property

Investment property purchased by the bank for trading purposes are recorded at historical cost at financial statement date less impairment losses, if any, according to CBY instructions.

3-7. Valuation of restricted investments

Murabaha transactions and other investments financed by restricted investment accounts are recorded on the same valuation bases mentioned above with related profits (losses) and related provisions are taken to restricted investment accounts net of the bank's share for managing these investments.

3-8. Valuation of assets for which titles have been transferred to the bank as a repayment of loans

Assets for which titles have been transferred to the bank or assets which the bank has otherwise taken possession are included in the balance sheet under "Debt balances and other assets" at the values carried by the bank less any decline in its values at the financial statements date. This decline is charged to the statement of income.

3-9. Contingent liabilities and commitments

Contingent liabilities, in which the bank is a party, are presented off balance sheet under "contingent liabilities and commitments" as they do not represent actual assets or liabilities at the balance sheet date.

3-10. Cash and cash equivalent

For the purpose of preparing the statement of cash flows, cash and cash equivalent consist of cash on hand, cash balances with Central Bank of Yemen, other than reserve balances, and demand deposits with other banks.

3-11. Property, equipment and depreciation

Property and equipment are stated at cost less accumulated depreciation and impairment losses, if any. Depreciation is charged to the statement of income on the straight-line method over the estimated useful life of property and equipment except land at the following rates:

**ISLAMIC BANK OF YEMEN FOR FINANCE AND INVESTMENT
SANA'A, REPUBLIC OF YEMEN**

**NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED DECEMBER 31, 2005**

	<u>Estimated useful lives</u>
Buildings	40 years
Equipment	5 - 8 years
Motor vehicles	5 years
Furniture and fixtures	5 - 33 years
Computer equipment	5 years

3.12. Impairment of assets

The Bank reviews the carrying amounts of the assets, according to its materiality, at the balance sheet date to determine whether there is any indication of impairment. If such indication exists, the assets' recoverable amount is estimated and compared with the carrying amount and any excess in the carrying amount is charged to the statement of income.

Any increase in the value of the assets is also recognized in the statement of income provided that the increase does not exceed the original recoverable value of the asset before impairment.

3.13. End of service bonus

End of service bonus is calculated for uninsured bank employees on the basis of one month salary for each year of service. These bonuses are recorded under "other provisions"

3-14. Taxation

- Corporate tax is calculated in accordance with the prevailing laws and regulations in Republic of Yemen.
- Due to the characteristics of the tax accounting in Yemen, provision for tax liabilities relating to deferred taxes is formed. In case of deferred tax assets, these assets are not certain to be realized in the near future. Accordingly, such assets are not recorded.

3-15. Statement of changes in restricted investments

Statement of changes in restricted investments present investments fully financed through funds received by the bank from restricted investment accounts. The bank manages restricted investments, as an agent for fees. The bank does not participate in the investment's outcome and the movement of restricted investments are presented in the statement of changes in restricted investments.

**ISLAMIC BANK OF YEMEN FOR FINANCE AND INVESTMENT
SANA'A, REPUBLIC OF YEMEN**

**NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED DECEMBER 31, 2005**

3-16. Prohibited revenues

Revenue prohibited by Islamic Sharia' (CBY interest on reserve balances) are recorded under "Credit balances and other liabilities" on the balance sheet. They are utilized in the areas approved by the bank's Sharia' Board

4. SUPERVISION OF CENTRAL BANK OF YEMEN

The bank's business activities are subject to the supervision of Central Bank of Yemen in accordance with the prevailing laws related to banks and Islamic banks.

5. SHARIA' BOARD

The bank's business activities are subject to the supervision of Sharia' Board consisting of 3 members appointed by the bank's general assembly. Their responsibilities are supervision of the sharia' aspects of the bank's activities according to Islamic sharia' regulations.

6. ZAKAT

Zakat is computed according to the Sharia' Board of the bank and collected from the shareholders. The amount collected is remitted to the related Governmental authority, which decides on the allocation of the Zakat.

7. FINANCIAL INSTRUMENTS AND MANAGING THEIR RELATED RISKS

7.1 Financial instruments

- a. The bank's financial instruments are represented in financial assets and liabilities. Financial assets include cash balances, current accounts, deposits with banks and financing of Murabaha, Mudaraba and Musharaka transactions and related debts. Financial liabilities include current and saving accounts, due to banks and investment accounts. Also, financial instruments include rights and obligations stated in contingent liabilities and commitments.

Note (3) to the financial statements includes significant accounting policies applied for recording and measuring significant financial instruments and their related revenues and expenses.

**ISLAMIC BANK OF YEMEN FOR FINANCE AND INVESTMENT
SANA'A, REPUBLIC OF YEMEN**

**NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED DECEMBER 31, 2005**

b. Fair value of financial instruments

Based on valuation bases of the bank's assets and liabilities stated in the notes to the financial statements, the fair value of the financial instruments do not differ fundamentally from their book values at the balance sheet date.

c. Forward contracts

The bank does not engage in forward contracts to meet its obligations in foreign currencies, nor does it engage in foreign exchange contracts to cover the risk of future settlement in foreign currencies.

7.2 *Managing related risks*

a. Return rate risk

Return due on unrestricted investment and saving accounts is determined on the basis of Mudaraba contract, which determines profit (loss) sharing basis during the period. Accordingly, any change in the profitability level will determine the return ratio that the bank could pay to unrestricted investment accounts holders. Therefore, the bank is not exposed, directly, to the risk of change in return rate.

b. Credit risk

Financing of Murabaha, Mudaraba and Musharaka transactions and their related debts, current accounts, deposits with banks and rights and obligations from others are considered financial assets exposed to credit risk. Credit risk represents the inability of these parties to meet their obligations when they fall due. In order to comply with CBY requirements (Circular No. 10 of 1997), the bank adheres to certain minimum standards in order to properly manage its credit risk as follows:

- Preparing credit studies on customers and banks before dealing with them and determining their related credit risk rating.
- Obtaining sufficient collaterals to minimize the credit risk exposure which may result in cases of insolvency of customers and banks.
- Following up and periodical reviews of customers and banks in order to evaluate their financial positions, credit rating and the required provision for non-performing debts.
- Distributing credit portfolio and investments over diversified sectors to minimize concentration or credit risk.

Note No. (40) to the financial statements indicates the distribution of assets, liabilities and contingent liabilities and commitments at balance sheet date.

**ISLAMIC BANK OF YEMEN FOR FINANCE AND INVESTMENT
SANA'A, REPUBLIC OF YEMEN**

**NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED DECEMBER 31, 2005**

c. Exchange rate risk

Due to the nature of the bank's activity, the bank deals in different foreign currencies, hence it is exposed to exchange rate risk. In order to minimize the exposure to exchange rate risk, the bank is trying to maintain balanced foreign currencies positions in compliance with the Central Bank of Yemen instructions and the requirements of CBY circular No. 6 of 1998 specifying that individual foreign currency position should not exceed 15% of the bank's capital and reserves, and that the aggregate open position for all foreign currencies should not exceed 25% of a bank's capital. Note (41) to the financial statement indicates the significant foreign currencies' positions at the balance sheet date.

8. CASH ON HAND AND RESERVE BALANCES WITH CENTRAL BANK OF YEMEN

	2005	2004
	<u>YR 000s</u>	<u>YR 000s</u>
Cash on hand - local currency	184,838	268,049
Cash on hand - foreign currency	<u>327,355</u>	<u>399,128</u>
	<u>512,193</u>	<u>667,177</u>
Reserve balance with CBY - local currency	632,318	733,270
Reserve balance with CBY - foreign currency	<u>2,521,799</u>	<u>1,846,506</u>
	<u>3,154,117</u>	<u>2,579,776</u>
	<u>3,666,310</u>	<u>3,246,953</u>

The reserve balances with Central Bank of Yemen represent the minimum reserve requirements against customers' accounts in Yemeni Rial and foreign currencies. These funds are not available for the Bank's daily business.

9. DUE FROM BANKS AND FINANCIAL INSTITUTIONS

	2005	2004
	<u>YR 000s</u>	<u>YR 000s</u>
a. Central Bank of Yemen		
Current accounts - local currency	118,687	721,332
Current accounts - foreign currency	<u>30,531</u>	<u>25,285</u>
	<u>149,218</u>	<u>746,617</u>
b. Local banks		
Current accounts	<u>213</u>	<u>7,301</u>
c. Foreign banks		
Current accounts	660,168	1,260,175
Investment deposits	<u>141,813</u>	<u>270,753</u>
	<u>801,981</u>	<u>1,530,928</u>
	<u>951,412</u>	<u>2,284,846</u>

**ISLAMIC BANK OF YEMEN FOR FINANCE AND INVESTMENT
SANA'A, REPUBLIC OF YEMEN**

**NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED DECEMBER 31, 2005**

10. FINANCING MURABAHA TRANSACTIONS (NET)

	<u>Note</u>	<u>2005</u> <u>YR 000s</u>	<u>2004</u> <u>YR 000s</u>
Financing Murabaha transactions - local		9,726,777	9,389,890
Financing Murabaha transactions - foreign		<u>175,364</u>	<u>280,624</u>
		9,902,141	9,670,514
Less:			
- Murabaha transactions provision	11	(1,501,329)	(876,843)
- Suspense revenues		(326,797)	(72,740)
- Deferred revenues		<u>(465,588)</u>	<u>(440,385)</u>
		7,608,427	8,280,546
Less: Transferred to restricted investments		<u>(771,508)</u>	<u>(1,182,637)</u>
		<u>6,836,919</u>	<u>7,097,909</u>

- Non-performing Murabaha transactions installments amounted to YR /2,199/ Million at 31/12/2005 (YR /1,630/ Million at 31/12/2004).
- The shortfall in Murabaha provision amounted to YR /746/ Million in addition to YR /799/ Million being the shortfall in the provision for debit balances and other assets at 31/12/2005.

11. FINANCING MURABAHA TRANSACTIONS PROVISION (NON-PERFORMING)

	<u>2005</u>			<u>2004</u>		
	<u>Specific</u> <u>YR 000s</u>	<u>General</u> <u>YR 000s</u>	<u>Total</u> <u>YR 000s</u>	<u>Specific</u> <u>YR 000s</u>	<u>General</u> <u>YR 000s</u>	<u>Total</u> <u>YR 000s</u>
Balance at beginning of the year	798,700	78,143	876,843	469,949	77,434	547,383
Used during the year	(5,982)	-	(5,982)	-	-	-
Provided during the year	397,616	-	397,616	113,843	709	114,552
Transfer from general to specific	78,143	(78,143)	-	-	-	-
Transfer from Mushraka	1,956	-	1,956	-	-	-
Transfer from Mudaraba	1,857	-	1,857	-	-	-
Transfer from contingent liabilities	22,330	-	22,330	-	-	-
Provided during the year (from credit balances)	<u>206,709</u>	<u>-</u>	<u>206,709</u>	<u>214,908</u>	<u>-</u>	<u>214,908</u>
	<u>1,501,329</u>	<u>-</u>	<u>1,501,329</u>	<u>798,700</u>	<u>78,143</u>	<u>876,843</u>

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**NOTES TO THE FINANCIAL STATEMENTS (continued)
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12. INVESTMENTS IN MUSHARAKA CONTRACTS (NET)

	<u>Note</u>	<u>2005</u> <u>YR 000s</u>	<u>2004</u> <u>YR 000s</u>
Taib Bank – external investment		104,040	99,100
Tadhamon International Islamic Bank – internal investment		<u>264,063</u>	<u>464,600</u>
		368,103	563,700
Less: Musharaka contracts provision	13	<u>(3,681)</u>	<u>(5,637)</u>
		<u>364,422</u>	<u>558,063</u>

13. MUSHRAKA CONTRACTS PROVISION (PERFORMING)

	<u>2005</u>			<u>2004</u>		
	<u>Specific</u> <u>YR 000s</u>	<u>General</u> <u>YR 000s</u>	<u>Total</u> <u>YR 000s</u>	<u>Specific</u> <u>YR 000s</u>	<u>General</u> <u>YR 000s</u>	<u>Total</u> <u>YR 000s</u>
Balance at beginning of the year	-	5,637	5,637	-	2,150	2,150
Provided during the year	-	-	-	-	3,487	3,487
Transfer to Murabaha	-	<u>(1,956)</u>	<u>(1,956)</u>	-	-	-
Balance at end of the year	<u>-</u>	<u>3,681</u>	<u>3,681</u>	<u>-</u>	<u>5,637</u>	<u>5,637</u>

14. INVESTMENTS IN MUDARABA CONTRACTS (NET)

	<u>Note</u>	<u>2005</u> <u>YR 000s</u>	<u>2004</u> <u>YR 000s</u>
Dallah Albaraka – external investment		487,845	613,217
Qatar Islamic Bank – external investment		<u>32,514</u>	<u>92,920</u>
		520,359	706,137
Less: Mudaraba contracts provision	15	<u>(5,204)</u>	<u>(7,061)</u>
		<u>515,155</u>	<u>699,076</u>

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**NOTES TO THE FINANCIAL STATEMENTS (continued)
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15. MUDARABA CONTRACTS PROVISION (PERFORMING)

	<u>2005</u>			<u>2004</u>		
	<u>Specific YR 000s</u>	<u>General YR 000s</u>	<u>Total YR 000s</u>	<u>Specific YR 000s</u>	<u>General YR 000s</u>	<u>Total YR 000s</u>
Balance at beginning of the year	-	7,061	7,061	-	641	641
Provided during the year	-	-	-	-	6,420	6,420
Transfer to Murabaha	-	(1,857)	(1,857)	-	-	-
Balance at end of the year	-	<u>5,204</u>	<u>5,204</u>	-	<u>7,061</u>	<u>7,061</u>

16. AVAILABLE FOR SALE INVESTMENTS

	<u>2005 YR 000s</u>	<u>2004 YR 000s</u>
Yemeni Center for Conciliation & Arbitration	230	230
Yemen Islamic Insurance Company	11,073	12,000
Financial Services Company	58,524	-
The Yemen Islamic Co. for Foam Manufacturing	<u>67,025</u>	<u>-</u>
	<u>136,852</u>	<u>12,230</u>

All available for sale investments are local investments.

17. INVESTMENT PROPERTY

	<u>2005 YR 000s</u>	<u>2004 YR 000s</u>
Artel Region Land	<u>276,161</u>	<u>-</u>

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**NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED DECEMBER 31, 2005**

18. DEBIT BALANCES AND OTHER ASSETS (NET)

	<u>Note</u>	<u>2005</u> <u>YR 000s</u>	<u>2004</u> <u>YR 000s</u>
Overdraft		1,595,111	1,966,564
Unpaid L/Cs		3,235,674	3,186,055
Assets which titles have been transferred to the Bank's ownership	3/8	86,756	-
Employees advances		32,748	31,577
Accrued income		43,643	60,667
Prepaid expenses		24,721	18,451
Stationary inventory		20,373	19,444
Others		<u>757,057</u>	<u>529,095</u>
		5,796,083	5,811,853
Less: provision for debit balance	19	(<u>440,685</u>)	(<u>444,814</u>)
		<u>5,355,398</u>	<u>5,367,039</u>

19. PROVISION FOR DEBIT BALANCES AND OTHER ASSETS

	<u>2005</u> <u>YR 000s</u>	<u>2004</u> <u>YR 000s</u>
Balance at beginning of the year	444,814	213,667
Provided during the year	-	234,452
Provision used during the year	(<u>4,129</u>)	(<u>3,305</u>)
Balance at the end of the year	<u>440,685</u>	<u>444,814</u>

20. PROPERTY AND EQUIPMENT (NET)

	<u>2005</u>			<u>2004</u>
	<u>Cost</u> <u>YR 000s</u>	<u>Accumulated</u> <u>Depreciation</u> <u>YR 000s</u>	<u>Net</u> <u>YR 000s</u>	<u>Net</u> <u>YR 000s</u>
Buildings	80,330	(1,601)	78,729	79,105
Equipment and machinery	125,651	(72,209)	53,442	74,740
Motor vehicles	51,507	(31,472)	20,035	17,001
Furniture and fixtures	155,661	(88,580)	67,081	55,268
Computers	<u>236,531</u>	(<u>168,251</u>)	<u>68,280</u>	<u>87,376</u>
Total	<u>649,680</u>	(<u>362,113</u>)	<u>287,567</u>	<u>313,490</u>

Depreciation for the year 2005 is YR / 69,267 / thousand (YR / 67,580 / thousand for the year 2004).

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**NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED DECEMBER 31, 2005**

21. CURRENT ACCOUNTS AND OTHER DEPOSITS

	<u>2005</u> <u>YR 000s</u>	<u>2004</u> <u>YR 000s</u>
Current accounts – local currency	737,720	2,490,696
Current accounts – foreign currency	<u>2,492,559</u>	<u>3,928,370</u>
	<u>3,230,279</u>	<u>6,419,066</u>
Cash margin – local currency	301,393	309,458
Cash margin – foreign currency	1,614,376	1,698,535
Other deposits	<u>30,305</u>	<u>86,353</u>
	<u>1,946,074</u>	<u>2,094,346</u>
	<u>5,176,353</u>	<u>8,513,412</u>

22. DUE TO BANKS AND FINANCIAL INSTITUTIONS

	<u>2005</u> <u>YR 000s</u>	<u>2004</u> <u>YR 000s</u>
Current accounts – foreign currency	<u>2,212,370</u>	<u>112,960</u>

23. CREDIT BALANCES AND OTHER LIABILITIES

	<u>Note</u>	<u>2005</u> <u>YR 000s</u>	<u>2004</u> <u>YR 000s</u>
Income tax for the year		-	6,998
Accrued expenses		95,720	102,108
Prohibited revenues by Islamic Shari'a	24	27,065	-
Other credit balances		<u>947,557</u>	<u>1,161,761</u>
		<u>1,070,342</u>	<u>1,270,867</u>

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**NOTES TO THE FINANCIAL STATEMENTS (continued)
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24. PROHIBITED REVENUES BY ISLAMIC SHARI'A

The following represent revenues from transactions prohibited by the Islamic Shaira' during the year, mainly interest on reserve balances with CBY, and its disbursement channels:

	<u>2005</u> <u>YR 000s</u>	<u>2004</u> <u>YR 000s</u>
Balance at the beginning of the year		
Donations	-	-
Resources		
Prohibited revenues by Islamic Sharia'a	334,788	230,399
Uses		
Donation	(101,014)	(15,491)
Provided provision during the year	(206,709)	(214,908)
Balance at the end of the year	<u>-</u>	<u>-</u>

25. OTHER PROVISIONS

	<u>2005</u>				
	<u>Balance at beginning of the year</u> <u>YR 000s</u>	<u>Provided during the year</u> <u>YR 000s</u>	<u>Used during the year</u> <u>YR 000s</u>	<u>Transfer to Murabaha</u> <u>YR 000s</u>	<u>Balance at end of the year</u> <u>YR 000s</u>
Provision for contingent liabilities	151,338	-	-	(22,330)	129,008
Provision for end of service compensation	<u>8,057</u>	<u>13,816</u>	<u>(8,872)</u>	<u>-</u>	<u>13,001</u>
	<u>159,395</u>	<u>13,816</u>	<u>(8,872)</u>	<u>(22,330)</u>	<u>142,009</u>
	<u>2004</u>				
	<u>Balance at beginning of the year</u> <u>YR 000s</u>	<u>Provided during the year</u> <u>YR 000s</u>	<u>Used during the year</u> <u>YR 000s</u>	<u>Balance at end of the year</u> <u>YR 000s</u>	
Provision for contingent liabilities	127,812	23,526	-	151,338	
Provision for end of service compensation	<u>7,267</u>	<u>7,956</u>	<u>(7,166)</u>	<u>8,057</u>	
	<u>135,079</u>	<u>31,482</u>	<u>(7,166)</u>	<u>159,395</u>	

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**NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED DECEMBER 31, 2005**

26. UNRESTRICTED INVESTMENT AND SAVING ACCOUNTS' HOLDERS

	<u>2005</u> <u>YR 000s</u>	<u>2004</u> <u>YR 000s</u>
Unrestricted investment deposits – local currency	3,278,837	3,531,209
Unrestricted investment deposits – foreign currency	<u>1,919,498</u>	<u>1,906,714</u>
	<u>5,198,335</u>	<u>5,437,923</u>
Saving deposits – local currency	1,071,430	1,168,627
Saving deposits – foreign currency	<u>776,254</u>	<u>809,000</u>
	<u>1,847,684</u>	<u>1,977,627</u>
Return of unrestricted investment and savings accounts	<u>643,000</u>	<u>502,000</u>
	<u>7,689,019</u>	<u>7,917,550</u>

27. CAPITAL

The capital of the Bank is YR /2.2/Billion represented in /2.2/Million shares of a par value of YR /1,000/ each according to the extra-ordinary General Assembly meeting decision on October 3, 2005 to raise capital through general reserve and retained earnings by YR /209/ Million and YR /11/ Million respectively in addition to a cash increase of YR /730/ Million offered only to existing shareholders. The following shows capital at December 31, 2005:

	<u>YR 000s</u>
Capital	2,200,000
Less: Unsubscribed amounts	<u>(225,703)</u>
Paid-up capital	<u>1,974,297</u>

28. RESERVES

	<u>2005</u> <u>YR 000s</u>	<u>2004</u> <u>YR 000s</u>
Statutory reserve	142,607	142,607
General reserve	<u>-</u>	<u>209,000</u>
	<u>142,607</u>	<u>351,607</u>

According to the Law and the Bank's Articles of Association, 15% of net profit for the year is transferred to statutory reserve till it equals two times paid-up capital.

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**NOTES TO THE FINANCIAL STATEMENTS (continued)
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29. RETURN OF UNRESTRICTED INVESTMENT AND SAVING ACCOUNTS HOLDERS

The share of unrestricted investment and saving accounts holders is determined by distributing total return between shareholders and customers based on the percentage of their contributions weighted by numbers. This calculation is proposed by the budget committee and approved by the Board of Directors. The investment return is as follows:

	<u>2005</u>		<u>2004</u>	
	<u>Yemeni Rial %</u>	<u>Foreign Currency %</u>	<u>Yemeni Rial %</u>	<u>Foreign Currency %</u>
Unrestricted deposits	13.65	4.55	11.58	3.52
Deposits for one year	12.80	4.26	10.89	3.30
Deposits for 9 months	11.94	3.98	10.14	3.08
Deposits for 6 months	10.24	3.41	8.69	2.64
Deposits for 3 months	9.38	3.13	7.96	2.42
Saving accounts	8.53	2.84	7.24	2.20

30. CONTINGENT LIABILITIES AND COMMITMENTS

	<u>2005 YR 000s</u>	<u>2004 YR 000s</u>
Letters of credit	8,709,069	13,186,728
Letters of guarantee	5,672,206	4,908,139
Other	<u>434,876</u>	<u>747,317</u>
	14,816,151	18,842,184
Less: Margin held	<u>(1,915,378)</u>	<u>(2,007,993)</u>
	<u>12,900,773</u>	<u>16,834,191</u>

31. REVENUES OF FINANCING MURABAHA TRANSACTIONS

	<u>2005 YR 000s</u>	<u>2004 YR 000s</u>
Revenues of Murabaha transactions – local	696,531	551,921
Revenues of Murabaha transactions – foreign	<u>-</u>	<u>5,666</u>
	<u>696,531</u>	<u>557,587</u>

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**NOTES TO THE FINANCIAL STATEMENTS (continued)
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32. REVENUES OF OTHER JOINT INVESTMENTS

	2005	2004
	<u>YR 000s</u>	<u>YR 000s</u>
Revenues of investments in Musharka contracts	75,908	44,006
Revenues of investment property	-	49,984
Revenues of investment deposits	<u>-</u>	<u>7,240</u>
	<u>75,908</u>	<u>101,230</u>

33. COMMISSIONS AND FEES INCOME ON BANKING SERVICES

	2005	2004
	<u>YR 000s</u>	<u>YR 000s</u>
Commissions on documentary credits	375,334	325,487
Commissions on letters of guarantee	91,540	59,723
Commissions on transfer of funds	41,356	29,262
Customers services charges	<u>111,219</u>	<u>195,398</u>
	<u>619,449</u>	<u>609,870</u>

34. GAINS OF FOREIGN CURRENCY TRANSACTIONS

	2005	2004
	<u>YR 000s</u>	<u>YR 000s</u>
Profit of dealing in foreign currencies	112,475	56,499
Gain from revaluation of foreign currencies	<u>149,275</u>	<u>100,985</u>
	<u>261,750</u>	<u>157,484</u>

35. OTHER OPERATING INCOME

	2005	2004
	<u>YR 000s</u>	<u>YR 000s</u>
Profit (loss) of disposal of property	421	(247)
Others	<u>19,456</u>	<u>7,862</u>
	<u>19,877</u>	<u>7,615</u>

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**NOTES TO THE FINANCIAL STATEMENTS (continued)
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36. PROVISIONS CHARGED TO STATEMENT OF INCOME

	<u>Note</u>	<u>2005 YR 000s</u>	<u>2004 YR 000s</u>
Murabaha provision	11	397,616	114,552
Mudaraba provision		-	6,420
Musharka provision		-	3,487
Qard Hasan provision		2,470	14
Debit balances and other assets provision	19	-	234,452
Contingent liabilities provision	25	-	23,526
End of service compensation provision	25	<u>13,816</u>	<u>8,057</u>
		<u>413,902</u>	<u>390,508</u>

37. GENERAL AND ADMINISTRATIVE EXPENSES AND DEPRECIATION

	<u>Note</u>	<u>2005 YR 000s</u>	<u>2004 YR 000s</u>
Wages and salaries		258,830	224,192
Depreciation of property & equipment	20	69,267	67,580
Insurance		16,360	18,404
Stationary		14,012	13,408
Communication		24,211	21,123
Water and electricity		9,092	10,813
Rent		20,507	20,342
Advertising		11,312	18,863
Transportation		48,426	47,446
Maintenance and fuel		22,636	19,862
Entertainment expenses		15,071	7,010
Taxes and duties		63,585	1,587
Professional fees		3,353	2,313
Zakat		45,809	39,239
Others		<u>21,282</u>	<u>37,836</u>
Total		<u>643,753</u>	<u>550,018</u>

38. EARNINGS PER SHARE

	<u>2005</u>	<u>2004</u>
Net profit for the year (YR thousand)	-	14,447
Less: Board of Directors' remuneration	<u>-</u>	<u>(1,450)</u>
	<u>-</u>	<u>12,997</u>
Weighted average of number of shares	<u>1,512</u>	<u>1,250</u>
Earnings per share (YR)	<u>-</u>	<u>10.40</u>

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**NOTES TO THE FINANCIAL STATEMENTS (continued)
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39. MATURITIES OF ASSETS AND LIABILITIES

	Due within 3 months YR Million	Due within 6 months YR Million	Due within 9 months YR Million	Due within one year YR Million	Due within more than one year YR Million	Total YR Million
a. Assets						
Due from banks and fin'l. institution	242	209	85	415	-	951
Murabaha financing contracts	4,889	2,495	548	898	1,072	9,902
Investments in Musharaka contracts	217	151	-	-	-	368
Investments in Mudaraba contracts	343	177	-	-	-	520
Available for sale investments	-	-	-	-	137	137
Investment property	-	-	-	-	276	276
Overdraft	399	399	399	398	-	1,595
Unpaid L/Cs	1,006	959	931	340	-	3,236
	7,096	4,390	1,963	2,051	1,485	16,985
b. Liabilities						
Current accounts and other deposits	5,176	-	-	-	-	5,176
Due to banks and fin'l. institution	2,212	-	-	-	-	2,212
Unrestricted investments	2,145	651	297	139	4,457	7,689
	9,533	651	297	139	4,457	15,077

**40. DISTRIBUTION OF ASSETS, LIABILITIES, AND CONTINGENT LIABILITIES
AND COMMITMENTS**

	Manufac- turing YR Million	Trade YR Million	Agricultural and Fishing YR Million	Financial YR Million	Individual and Others YR Million	Total YR Million
Assets						
Murabaha financing contracts	1,996	6,485	63	-	1,358	9,902
Investments in Musharaka contracts	-	-	-	368	-	368
Investments in Mudaraba contracts	-	-	-	520	-	520
Available for sale investments	-	-	-	137	-	137
Investment property	-	276	-	-	-	276
Liabilities						
Current accounts	602	1,049	-	-	1,579	3,230
Othe deposits	-	1,885	-	2	59	1,946
Due to banks and fin'l. instituion	-	-	-	2,212	-	2,212
Unrestricted investments	-	4,726	-	-	2,963	7,689
Contingent liabilities						
L/Gs	-	-	-	-	4,840	4,840
L/Cs	1,210	6,482	-	-	-	7,692
Others	-	208	-	-	160	368

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**NOTES TO THE FINANCIAL STATEMENTS (continued)
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41. SIGNIFICANT FOREIGN CURRENCIES' POSITIONS

To comply with CBY circular No. 6 of 1998, the bank establishes limits for positions in individual foreign currencies as well as an aggregate limitation for all currencies. These limits are 15% and 25% of capital and reserves respectively. The following schedule reflects the bank's significant foreign currencies positions at balance sheet date.

	<u>2005</u>		<u>2004</u>	
	<u>Surplus (deficit) YR 000's</u>	<u>% of capital & reserves</u>	<u>Surplus (deficit) YR 000's</u>	<u>% of capital & reserves</u>
US Dollar	526,937	25%	3,557,986	221%
EURO	(118,321)	(6%)	577,084	36%
Sterling Pound	(11,098)	(1%)	3,849	-
Saudi Arabia Rial	1,430	-	618,987	38%
Other	<u>616</u>	<u>-</u>	<u>964</u>	<u>-</u>
Surplus (deficit)	<u>399,564</u>	<u>19%</u>	<u>4,758,870</u>	<u>295%</u>

42. TRANSACTIONS WITH RELATED PARTIES

The bank in its ordinary activity deals with some companies owned by shareholders of the bank or the board of directors. These transactions represent Murabaha financing and other transactions. The balances of these transactions with related parties at the balance sheet date are as follows:

	<u>2005 YR Millions</u>	<u>2004 YR Millions</u>
Murabaha financing contracts	234	449
Debit balances and other assets	52	77
Unrestricted investment accounts	131	186
Current and saving accounts	1,053	427
Credit balances	181	126

43. TAXATION

- There is a legal dispute with the Tax Authority which was not settled until the financial statements preparation date regarding the Bank's profits (as well as all Islamic banks operating in Yemen) during the exemption period, ended on June 7, 2003, being subject to tax. The Bank's management believes that there is no liability on the Bank due to the strong position of the Bank and his tax exemption according to the prevailing laws.

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- The Bank submitted his voluntary tax declaration for the year 2004 in time and remitted the amount due.

44. ZAKAT POSITION

The Bank has submitted his zakat declaration for the year 2004 in time and remitted the amount due.

45. COMPARATIVE FIGURES

Some comparative figures have been reclassified to conform with this year financial statements presentation.
