International Investment Bank

Separate Financial Statements

Year ended 31 December 2011

Together with Independent Auditors' Report

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Independent auditors' report

To the Council of the International Investment Bank

We have audited the accompanying separate financial statements of the International Investment Bank (the "Bank"), which comprise the separate statement of financial position as at 31 December 2011, and the separate income statement, separate statement of comprehensive income, separate statement of changes in equity and separate statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the separate financial statements

Management is responsible for the preparation and fair presentation of these separate financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of separate 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 separate 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 separate financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the separate financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the separate 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 separate 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 Bank'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 separate 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 separate financial statements present fairly, in all material respects, the financial position of the International Investment Bank as at 31 December 2011, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Consolidated financial statements are presented separately

Without qualifying our opinion, we draw your attention to Note 2 to the separate financial statements which states that the International Investment Bank is a parent entity of the Group of the International Investment Bank and that the consolidated financial statements of the Group of the International Investment Bank prepared in accordance with International Financial Reporting Standards were authorized for release by the Bank's management separately. The consolidated financial statements of the Group of the International Investment Bank have not been audited.

21 March 2012

SEPARATE STATEMENT OF FINANCIAL POSITION

As at 31 December 2011

(Thousands of Euros)

	Note	*31 December 2011*	*31 December 2010 (restated)*	*1 January 2010 (restated)*
Assets				
Cash and cash equivalents	6	13,901	89,723	99,608
Deposits with banks and other financial institutions	7	111,244	30,052	40,063
Financial instruments at fair value through profit or loss:				
- Combined financial instruments	8	–	15,732	13,757
Available-for-sale investment securities	9	71,035	62,182	30,989
Held-to-maturity investment securities	10	423	407	377
Loans to customers	11	50,959	55,052	75,891
Assets held for sale	12	2,048	–	–
Investment property	13	50,287	47,951	15,667
Property and equipment	14	49,940	47,512	23,105
Other assets	15	1,451	2,138	1,491
Total assets		**351,288**	**350,749**	**300,948**
Liabilities				
Due to banks and other financial institutions	16	1	982	58
Current customer accounts		2,382	2,254	2,425
Financial instruments at fair value through profit or loss:				
- Financial instruments held for trading		–	–	21
Other liabilities	15	5,773	6,376	4,991
Total liabilities		**8,156**	**9,612**	**7,495**
Equity	17			
Subscribed capital		1,300,000	1,300,000	1,300,000
Callable capital		(1,085,505)	(1,085,505)	(1,085,505)
Paid-in capital		**214,495**	**214,495**	**214,495**
Revaluation reserve for investment securities available-for-sale		(2,351)	553	3,951
Revaluation reserve for property and equipment		31,091	27,845	–
Retained earnings at the beginning of the year		98,244	75,007	14,720
Net income for the year		1,653	23,237	60,287
Total equity		**343,132**	**341,137**	**293,453**
Total equity and liabilities		**351,288**	**350,749**	**300,948**

Signed and authorized for release on behalf of the Board of the Bank

Vasily V. Kirpichev Chairman of the Board

Eugeny Atanassov Managing Director of the Financial Department

15 March 2012

The accompanying notes are an integral part of these separate financial statements.

SEPARATE INCOME STATEMENT

Year ended 31 December 2011

(Thousands of Euros)

	Note	*2011*	*2010 (restated)*
Interest income	21	8,565	10,557
Interest expenses	21	(55)	(9)
Net interest income		**8,510**	**10,548**
(Allowance) for loan impairment	11	(3,846)	(15,393)
Net interest income/(expense) after allowance for loan impairment		**4,664**	**(4,845)**
Fee and commission income		292	361
Fee and commission expense		(69)	(80)
Net fee and commission income		**223**	**281**
Net (losses)/gains from foreign currencies	22	(151)	854
Net gains/(losses) from financial instruments at fair value through profit or loss			
- *Financial instruments held for trading*		–	(50)
- *Combined financial instruments*		2,174	1,970
Net gains from available-for-sale investment securities		428	3,014
Income from lease of investment property	13	6,763	6,153
Net gains from revaluation of investment property	13	1,755	28,982
Other income		78	122
Net non-interest income		**11,047**	**41,045**
Operating income		**15,934**	**36,481**
(Provision) for impairment of other assets		(2)	(133)
General and administrative expenses	23	(12,865)	(12,444)
Other operating expenses		(1,414)	(667)
Operating expense		**(14,281)**	**(13,244)**
Net income for the year		**1,653**	**23,237**

The accompanying notes are an integral part of these separate financial statements.

SEPARATE STATEMENT OF COMPREHENSIVE INCOME

Year ended 31 December 2011

(Thousands of Euros)

	2011	*2010*
Net income for the year	**1,653**	**23,237**
Other comprehensive income/(expense)		
Net losses from revaluation of available-for-sale investment securities	(2,904)	(3,398)
Revaluation of property and equipment	3,246	27,845
Total other comprehensive income	**342**	**24,447**
Total comprehensive income for the year	**1,995**	**47,684**

The accompanying notes are an integral part of these separate financial statements.

SEPARATE STATEMENT OF CHANGES IN EQUITY

Year ended 31 December 2011

(Thousands of Euros)

	Subscribed capital	*Callable capital*	*Revaluation reserve for investment securities available for sale*	*Revaluation reserve for property and equipment*	*Retained earnings*	*Total equity*
At 31 December 2009	**1,300,000**	**(1,085,505)**	**3,951**	–	**75,007**	**293,453**
Total comprehensive income	–	–	(3,398)	27,845	23,237	**47,684**
At 31 December 2010	**1,300,000**	**(1,085,505)**	**553**	**27,845**	**98,244**	**341,137**
Total comprehensive income	–	–	(2,904)	3,246	1,653	**1,995**
At 31 December 2011	**1,300,000**	**(1,085,505)**	**(2,351)**	**31,091**	**99,897**	**343,132**

The accompanying notes are an integral part of these separate financial statements.

SEPARATE STATEMENT OF CASH FLOWS

Year ended 31 December 2011

(Thousands of Euros)

	Note	*2011*	*2010 (restated)*
Cash flows from operating activities			
Interest, fees and commissions received from loans to customers and deposits with banks and other financial institutions		6,134	7,018
Interest received from combined financial instruments		757	2,295
Interest, fees and commissions paid		(116)	(89)
Net receipts from trading in foreign currencies		15	(28)
General and administrative expenses		(10,109)	(10,427)
Other operating expenses arising from banking transactions		(1,414)	(667)
Cash flows from lease of investment property		6,763	6,153
Cash flows from operating activities before changes in operating assets and liabilities		**2,030**	**4,255**
Net (increase)/decrease in operating assets			
Deposits with banks and other financial institutions		(81,308)	10,111
Combined financial instruments		17,907	–
Loans to customers		(628)	6,603
Assets held for sale		(2,043)	–
Other assets		700	(333)
Net increase/(decrease) in operating liabilities			
Due to banks and other financial institutions		(1,017)	940
Current customer accounts		121	(194)
Other liabilities		(551)	804
Net cash (used in) / flows from operating activities		**(64,789)**	**22,186**
Cash flows from investing activities			
Purchase of available-for-sale investment securities		(58,151)	(133,732)
Proceeds from sale and redemption of available-for-sale investment securities		49,314	103,596
Investments in investment property		(581)	(673)
Acquisition of property and equipment		(1,655)	(1,171)
Net cash flows used in investing activities		**(11,073)**	**(31,980)**
Effect of exchange rate changes on cash and cash equivalents		40	(91)
Net decrease in cash and cash equivalents		**(75,822)**	**(9,885)**
Cash and cash equivalents, beginning		**89,723**	**99,608**
Cash and cash equivalents, ending	6	**13,901**	**89,723**

The accompanying notes are an integral part of these separate financial statements.

(Thousands of Euros)

1. Principal activities

The International Investment Bank (the "Bank") was founded in 1970 and has operated since 1 January 1971.

The Bank is an international institution operating on the basis of the Intergovernmental Agreement on the Establishment of the International Investment Bank (the "Agreement") and the Statutes. The Agreement was ratified by the member countries of the Bank and registered with the Secretariat of the United Nations in December 1971. The Bank is primarily engaged in commercial lending for the benefit of national investment projects in the member countries of the Bank and for other purposes defined by the Council of the Bank. The Bank also performs transactions with securities and foreign currency. The Bank operates from its office at 7 Mashi Poryvaevoi St., Moscow, Russia.

The Bank had an average of 148 staff employees during 2011 (2010: 148).

Member countries of the Bank

The member countries of the Bank include:

Member countries	*2011* %	*2010* %
Russian Federation	44.704	44.704
Republic of Poland*	13.590	13.590
Czech Republic	9.697	9.697
Republic of Bulgaria	9.526	9.526
Republic of Hungary*	9.369	9.369
Romania	5.892	5.892
Slovak Republic	4.849	4.849
Republic of Cuba	1.711	1.711
Mongolia	0.335	0.335
Socialist Republic of Vietnam	0.327	0.327
	100.000	**100.000**

* Republic of Poland and Republic of Hungary announced their withdrawal from membership in the Bank in 1999 and 2000, respectively, and are no longer full members of the Bank. The Bank is in the process of negotiating mutual obligations with these countries.

In accordance with the Agreement, each member country of the Bank may withdraw from membership upon notice to the Council of the Bank at least six months in advance. In this case the Bank must settle all obligations to the relevant member country.

The member countries of the Bank may vote at the annual and general meetings of the Council and each member country has one vote regardless of the size of its contribution to the Bank's capital.

Conditions of the Bank's financial and business operations in the member countries

In accordance with the Agreement, the Bank's assets, regardless of location, have immunity from any administrative or judicial interference.

In the member countries, the Bank is not subject to taxation and enjoys all privileges available to diplomatic representations.

The Bank is not subject to regulation by the Central Banks of the member countries, including the country of residence.

Business environment in the member countries

The member countries have experienced political and economic change, which has affected, and may continue to affect, the activities of enterprises operating in these countries. Consequently, operations in some member countries involve risks, which do not typically exist in developed markets.

The accompanying separate financial statements reflect the management's assessment of the impact of the member countries' business environment on the results of operations and financial position of the Bank. Future evolution of the conditions in which the Bank operates may differ from the assessment made by the management for the purposes of these separate financial statements.

(Thousands of Euros)

2. Basis of preparation

General

The Bank, as a parent company, prepares consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS") approved by the International Accounting Standards Board. The consolidated financial statements of the Group of the International Investment Bank for the year ended 31 December 2011 have been signed and authorized for release on behalf of the Board on 15 March 2012 and are available for review at the Bank's office at 7 Mashi Poryvaevoi St., Moscow.

These financial statements have been prepared on a separate basis in accordance with International Financial Reporting Standards ("IFRS"). The separate financial statements have been prepared to be included in the report on activities of the International Investment Bank for 2011, which is to be submitted for consideration of the Revision Commission and the meeting of the Bank's Board.

Subsidiaries

As at 31 December 2011, the Bank controlled LLC StroyProektInvest as a holder of a 100% interest in the company's share capital. LLC StroyProektInvest is a limited liability company operating in accordance with the laws and regulations of the Russian Federation. The interest was acquired in June 2011 as part of bad debt workout. The Bank is planning to sell the interest during the first quarter of 2012. The company is principally engaged in construction works.

Basis of measurement

These separate financial statements have been prepared under the historical cost convention with the exception of the financial instruments under fair value convention, the changes of which are translated through profit or loss account for the period, available-for-sale financial instruments also stated at fair value, and buildings and investment property are stated at revalued amounts.

Preparation and presentation of financial statements

In accordance with the Statutes of the Bank, the financial year begins on 1 January and ends on 31 December.

Functional and presentation currency

The management has determined the Bank's functional and presentation currency to be the EURO ("EUR") as it reflects the economic substance of the underlying operations conducted by the Bank and circumstances affecting its operations, because most financial assets and financial liabilities as well as income and expenses of the Bank are denominated in EUR.

These separate financial statements are presented in thousands of Euros ("Thousands of Euros"), unless it is indicated otherwise.

3. Summary of accounting policies

The accounting policies adopted are consistent with those used in the previous financial year except for the following:

Changes in accounting policies

The Bank has adopted the following amended IFRS and new IFRIC Interpretations during the year. The principal effects of these changes are as follows:

IAS 24, Related Party Disclosures (Revised)
The revised IAS 24, issued in November 2009, simplifies the disclosure requirements for government-related entities and clarifies the definition of a related party. Previously, an entity controlled or significantly influenced by a government was required to disclose information about all transactions with other entities controlled or significantly influenced by the same government. The revised standard requires disclosure about these transactions only if they are individually or collectively significant. The revised IAS 24 is effective for annual periods beginning on or after 1 January 2011, with earlier application permitted. The adoption of the revised standard had no impact on the Bank's separate financial statements.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Changes in accounting policies (continued)

Amendment to IAS 32, Financial instruments: Presentation – Classification of Rights Issues
The amendment was issued by the IASB in October 2009 and is effective for annual periods beginning on or after 1 February 2010. The amendment alters the definition of a financial liability to classify rights issues as equity instruments. This is applicable if the rights are given *pro rata* to all of the existing owners of the same class of an entity's non-derivative equity instruments, in order to acquire a fixed number of the entity's own equity instruments for a fixed amount in any currency. This amendment had no impact on the Bank's separate financial statements.

IFRIC 19, Extinguishing Financial Liabilities with Equity Instruments
IFRIC Interpretation 19 was issued in November 2009 and is effective for annual periods beginning on or after 1 July 2010. The Interpretation clarifies the accounting when the terms of a financial liability are renegotiated and result in the entity issuing equity instruments to a creditor to extinguish all or part of the financial liability. This amendment had no impact on the Bank's separate financial statements.

Improvements to IFRSs
In May 2010, the IASB issued the third omnibus of amendments to its standards, primarily with a view to removing inconsistencies and clarifying wording. Most of the amendments are effective for annual periods beginning on or after 1 January 2011. There are separate transitional provisions for each standard. Amendments included in these Improvements to IFRS had an impact on the accounting policies, financial position or performance of the Bank as described below:

- IFRS 7, *Financial Instruments*: *Disclosures*: introduces the amendments to quantitative and credit risk disclosures. The additional requirements had minor impact as the required information was readily available.
- Other amendments to IFRS 1, IFRS 3, IAS 1, IAS 27, IAS 34 and IFRIC 13 will have no impact on the accounting policies, financial position or performance of the Bank.

The following amended standards and interpretations had no impact on accounting policies, financial position or performance of the Bank:

- IFRS 1, *First-time Adoption of International Financial Reporting Standards – Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters*
- IFRIC 14, *Prepayments of a Minimum Funding Requirement*

Foreign currency transactions

For the purposes of these separate financial statements, any currency other than the Euro is treated as a foreign currency. Foreign currency transactions are recorded in the functional currency at the exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated to the functional currency at the exchange rate ruling at the reporting date. Gains and losses arising from foreign exchange differences are recognized in the separate income statement as net (losses)/gains from foreign currencies. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated to the functional currency at the exchange rate ruling at the date of the initial transaction. Non-monetary assets and liabilities that are recorded at fair value in a foreign currency are translated to the euro at the exchange rate ruling at the date when their fair value was measured.

Differences between the contractual exchange rate of a transaction in a foreign currency and the Bank's official exchange rate at the date of the transaction are included in net (losses)/gains from foreign currencies.

Subsidiaries and associates

Subsidiaries are those entities, in which the Bank has an interest of more than one half of the voting rights or equity interest, or otherwise has power to exercise control over their operations. Associates are entities in which the Bank generally has between 20% and 50% of the voting rights or equity interest, or is otherwise able to exercise significant influence, but which it does not control or jointly control. These financial statements of the Bank contain no consolidated interests of the Bank and no investments recognized under the equity method.

Investments in subsidiaries and associates are carried in the separate financial statements at acquisition cost. Management regularly measures the recoverable value of such investments and, when necessary, provides for impairment.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Cash and cash equivalents

Cash and cash equivalents include cash on hand, Nostro accounts due from banks and other financial institutions and short-term deposits with banks, including reverse repurchase agreements, which mature within ninety days from the origination date and are free from contractual encumbrances.

Financial instruments

Recognition

Financial assets in the scope of IAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, available-for-sale financial assets, as appropriate. When financial assets are recognized initially, they are measured at fair value. In the case of investments not classified as financial assets at fair value through profit or loss, directly attributable transaction costs are added to their fair value. The Bank determines the classification of its financial assets upon initial recognition, and subsequently can reclassify financial assets in certain cases as described below.

Financial assets and liabilities are recorded in the separate statement of financial position when the Bank becomes a party to the contractual provisions of the instrument. All regular way purchases and sales of financial assets are recognized on the transaction date, i.e. the date that the Bank commits to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

'Day 1' profit

Where the transaction price in a non-active market is different to the fair value from other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable markets, the Bank immediately recognizes the difference between the transaction price and fair value (a ‘Day 1’ profit) in the separate income statement. In cases where use is made of data which is not observable, the difference between the transaction price and model value is only recognized in the separate income statement when the inputs become observable, or when the instrument is derecognized.

Classification of financial instruments

Financial instruments at fair value through profit or loss are those financial assets and liabilities that are:

- Acquired or incurred principally for the purpose of selling or repurchasing in the near term;
- Part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking;
- Derivative financial instruments (except for derivative financial instruments that are designated and effective hedging instruments) and held for trading; or
- Upon initial recognition, are designated by the Bank as at fair value through profit or loss.

The Bank designates financial assets and liabilities at fair value through profit or loss if:

- The assets or liabilities are managed and evaluated on a fair value basis;
- The designation eliminates or significantly reduces an accounting mismatch which would otherwise arise; or
- The asset or liability is a combined financial instrument, i.e., contains an embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

The fair values are estimated based on quoted market prices or pricing models that take into account the current market and contractual prices of the underlying instruments and other factors.

Derivative financial instruments held for trading that are in a net receivable position (positive fair value) as well as option contracts acquired are reported as assets in the separate financial statements. Derivative financial instruments held for trading that are in a net payable position (negative fair value) as well as option contracts issued are reported as liabilities in the separate financial statements. Gains and losses resulting from these instruments are included in the separate income statement as net gains/(losses) from financial instruments at fair value through profit or loss.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Financial instruments (continued)

An embedded derivative is separated from the host contract and it is accounted for as a derivative if, and only if the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract, a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and the combined instrument is not measured at fair value with changes in fair value recognized in profit or loss for the period. Derivatives embedded in financial assets or financial liabilities at fair value through profit or loss are not separated.

Financial assets and liabilities at fair value through profit or loss in the separate income statement for the period are not reclassified after initial recognition. Interest income on financial assets at fair value through profit or loss is recognized in the separate income statement as interest income.

Held-to-maturity financial assets are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Bank has the positive intention and ability to hold to maturity, other than:

- Held-to-maturity financial assets that the Bank designates as at fair value through profit or loss upon initial recognition;
- Held-to-maturity financial assets that the Bank designates as available for sale upon initial recognition; or
- Held-to-maturity financial assets that meet the definition of loans and accounts receivable.

Financial assets which the Bank intends to hold for an undefined period are not included in this classification. Held-to-maturity financial assets are subsequently measured at amortized cost. Gains and losses are recognized in the separate income statement when the investments are impaired, as well as through the amortization process.

Loans and accounts receivable are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than:

- Loans and accounts receivable that the Bank intends to sell immediately or in the near term;
- Loans and accounts receivable that the Bank designates as at fair value through profit or loss upon initial recognition;
- Loans and accounts receivable that are designated as available for sale upon initial recognition; or
- Loans and accounts receivable for which the Bank may not substantially recover all of its initial investment, other than because of credit deterioration.

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Such assets are carried at amortized cost using the effective interest method. Gains and losses are recognized in the separate income statement when such assets are derecognized or impaired, as well as through the amortization process.

Available-for-sale financial assets are those non-derivative financial assets that are designated as available for sale or are not classified in any of the three preceding categories. After initial recognition available-for-sale financial assets are measured at fair value with gains and losses being recognized in other comprehensive income until the investment is derecognized or until the investment is determined to be impaired, at which time the cumulative gains and losses previously recognized in other comprehensive income are reclassified to the separate income statement. However, interest calculated using the effective interest method is recognized in the consolidated income statement.

Fair value measurement principles

The fair value of financial instruments traded in an active market at the reporting date is based on their quoted market price or dealer price quotations (bid price for long positions and ask price for short positions), without any deduction for transaction costs.

For all other financial instruments not listed in an active market, the fair value is determined by using appropriate valuation techniques. Valuation techniques include net present value techniques, comparison to similar instruments for which market observable prices exist, options pricing models and other relevant valuation models.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Financial instruments (continued)

Offsetting

Financial assets and liabilities are offset and the net amount is reported in the separate statement of financial position when there is a legally enforceable right to set off the recognized amounts, and there is an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously. This is not generally the case with master netting agreements, and the related assets and liabilities are presented gross in the separate statement of financial position.

Reclassification of financial assets

If a non-derivative financial asset classified as held for trading is no longer held for the purpose of selling in the near term, it may be reclassified out of the fair value through profit or loss category in one of the following cases:

- a financial asset that would have met the definition of loans and receivables above may be reclassified to loans and receivables category if the Bank has the intention and ability to hold it for the foreseeable future or until maturity;
- other financial assets may be reclassified to available-for-sale or held-to-maturity categories only in rare circumstances.

A financial asset classified as available for sale that would have met the definition of loans and receivables may be reclassified to loans and receivables category if the Bank has the intention and ability to hold it for the foreseeable future or until maturity.

Financial assets are reclassified at their fair value at the date of reclassification. Any gain or loss previously recognized in profit or loss is not reversed. The fair value of the financial asset at the date of reclassification becomes its new cost or amortized cost, as applicable.

Repurchase and reverse repurchase agreements and securities lending

Sale and repurchase agreements ("repo") are treated as secured financing transactions. Securities sold under sale and repurchase agreements are retained in the separate statement of financial position and, in case the transferee has the right by contract or custom to sell or repledge them, reclassified as securities pledged under sale and repurchase agreements. The corresponding liability is presented within amounts due to credit institutions or customers. Securities purchased under agreements to resell ("reverse repo") are recorded as cash equivalents, amounts due from credit institutions or loans to customers, as appropriate. The difference between sale and repurchase price is treated as interest and accrued over the life of repo agreements using the effective yield method.

Securities lent to counterparties are retained in the separate statement of financial position. Securities borrowed are not recorded in the separate statement of financial position unless they are sold to third parties, in which case the purchase and sale are recorded within gains less losses from trading securities in the separate income statement. The obligation to return them is recorded at fair value as a trading liability.

Leases

Operating leases – Bank as lessee

Leases of assets under which the risks and rewards of ownership are effectively retained with the lessor are classified as operating leases. Lease payments under an operating lease are recognized as expenses on a straight-line basis over the lease term and included in general and administrative expenses.

Operating leases – Bank as lessor

The Bank presents assets subject to operating leases in the separate statement of financial position according to the nature of the asset. Lease income from operating leases is recognized in net non-interest income in the separate income statement on a straight-line basis over the lease term as income from lease of investment property. The aggregate cost of incentives provided to lessees is recognized as a reduction of rental income on a straight-line basis over the lease term. Initial direct costs incurred specifically to earn revenues from an operating lease are added to the carrying amount of the leased asset.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Impairment of financial assets

The Bank assesses at each reporting date whether there is objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event (or events) has an impact on the estimated future cash flows from the financial asset or the group of financial assets that can be reliably estimated.

Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganization and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Financial assets carried at amortized cost

For deposits with banks and other financial institutions, held-to-maturity investment securities, loans to customers that are carried at amortized cost the Bank assesses individually whether objective evidence of impairment exists for the financial assets.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's amount recorded in the separate statement of financial position and the present value of estimated future cash flows (excluding expected future credit losses that have not yet been incurred). The amount of the asset recorded in the separate statement of financial position is reduced through the use of an allowance account and the amount of the loss is recognized in the separate income statement. Interest income continues to be accrued on the reduced carrying amount of the asset based on the original effective interest rate of the asset. Financial asset together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realized or has been transferred to the Bank. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is increased or reduced by adjusting the allowance account. If earlier write-offs are later recovered, such the recovery is credited in the separate income statement.

The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate. If a financial asset has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate. The calculation of the present value of the estimated future cash flows of a collateralized financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Available-for-sale financial instruments

For financial instruments available-for-sale, the Bank assesses at each reporting date whether there is objective evidence that an instrument or a group of instruments is impaired.

In the case of equity investments classified as available for sale, objective evidence of impairment would include a significant or prolonged decline in the fair value of the investment below its acquisition cost. Where there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognized in the separate income statement – is reclassified from other comprehensive income to the separate income statement. Impairment losses on equity investments are not reversed through the separate income statement; increases in their fair value after impairment are recognized directly in other comprehensive income.

In the case of debt instruments classified as available for sale, impairment is assessed based on the same criteria as financial assets carried at amortized cost. Interest income is based on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded in the separate income statement. If, in a subsequent year, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in the separate income statement, the impairment loss is reversed through the separate income statement.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Impairment of financial assets (continued)

Renegotiated loans

Where possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. The accounting treatment of such restructuring is as follows:

- If the currency of the loan has been changed, the old loan is derecognized and the new loan is recognized in the separate statement of financial position;
- If the loan restructuring is not caused by the financial difficulties of the borrower, the Bank uses a similar approach as in respect of the derecognition of financial liabilities described below;
- If the loan restructuring is due to the financial difficulties of the borrower and the loan is deemed impaired after this restructuring, the Bank recognizes the difference between the present value of the future cash flows discounted using the original effective interest rate and the carrying amount before the restructuring as an expense for impairment in the reporting period. If the loan is not impaired after the restructuring, the Bank restates the effective interest rate.

Once the terms have been renegotiated, the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an impairment assessment, calculated using the loan's original or current effective interest rate.

Derecognition

Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognized in the separate statement of financial position where:

- The rights to receive cash flows from the asset have expired;
- The Bank has transferred its rights to receive cash flows from the asset, or retained the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass-through' arrangement; and
- The Bank either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Bank has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognized to the extent of the Bank's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Bank's continuing involvement is the amount of the transferred asset that the Bank may repurchase, except that in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, the extent of the Bank's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

Financial liabilities

A financial liability is derecognized when the obligation under the liability is discharged or cancelled or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognized in the separate income statement.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Investment property

Investment property is property that is not used in the Bank's operations and is held by the Bank to earn rentals under operating lease or yield from an increase in its fair value. Investment property is carried at fair value with changes in its fair value recognized in the separate income statement. Gains and losses resulting from changes in the fair value of investment property are taken to the financial result and recorded as gains or losses from revaluation and disposal of investment property.

Subsequent costs are capitalized only when it is probable that future economic benefits will flow from the asset and its value can be measured reliably. If there is a change in use of an investment property, it is reclassified to property and equipment, and its carrying amount at the date of reclassification becomes its deemed cost to be subsequently depreciated.

Property and equipment

Property and equipment are carried in the separate financial statements at cost, less costs of day-to-day servicing, accumulated depreciation and accumulated impairment losses, excluding buildings that are recorded at revalued amounts, as described below. Such cost includes the cost of replacing part of equipment when that cost is incurred if the recognition criteria are met.

The carrying amount of property and equipment is reviewed for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable.

Where an item of property and equipment comprises major components having different useful lives, they are accounted for as separate items of property and equipment.

Buildings are carried at a revalued amount, which is the fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Valuations of buildings are performed frequently enough to ensure that the fair value of a revalued asset does not differ materially from its carrying amount.

Accumulated depreciation as at the revaluation date is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset. Any revaluation surplus is recognized in other comprehensive income, except to the extent that it reverses a revaluation deficit of the same asset previously recognized in the separate income statement, in which case the increase is recognized in the separate income statement. A revaluation deficit is recognized in the separate income statement, except that a deficit directly offsetting a previous surplus on the same asset is directly offset against the surplus in the revaluation reserve for property and equipment.

Upon disposal, any revaluation reserve relating to the particular asset being sold is transferred to retained earnings.

Depreciation of property and equipment (including self-constructed property and equipment) is charged to the separate income statement on a straight-line basis over their estimated useful lives from the date when property and equipment become available for use. The useful lives are as follows:

	Years
Buildings	50
Equipment	3-7
Computers	3-6
Office furniture	5-10
Vehicles	4

The asset's residual values, useful lives and depreciation methods are reviewed, and adjusted as appropriate, at each financial year-end.

Costs related to repairs and renewals are charged when incurred and included in general and administrative expenses, unless they qualify for capitalization.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Intangible assets

Intangible assets include computer software.

Intangible assets acquired by the Bank are carried at cost, less accumulated amortization and accumulated impairment losses.

Amortization of intangible assets is charged to the separate income statement on a straight-line basis over the estimated useful lives of intangible assets.

	Years
Software	3

Assets classified as held for sale

The Bank classifies a non-current asset as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. For this to be the case, the non-current asset must be available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets and its sale must be highly probable.

The sale qualifies as highly probable if the Bank's management is committed to a plan to sell the non-current asset and an active program to locate a buyer and complete the plan must have been initiated. Further, the non-current asset must have been actively marketed for a sale at price that is reasonable in relation to its current fair value and in addition the sale should be expected to qualify for recognition as completed within one year from the date of classification of the non-current asset as held for sale.

The Bank measures an asset classified as held for sale at the lower of its carrying amount and fair value less costs to sell. The Bank recognizes an impairment loss for any initial or subsequent write-down of the asset to fair value less costs to sell if events or changes in circumstances indicate that their carrying amount may be impaired.

Interest-bearing liabilities

Interest-bearing liabilities are initially recognized at cost being their initial amount less transaction costs incurred. Subsequently, interest-bearing liabilities are carried at amortized cost, recognizing the difference between the actual amount of funds raised and the price of settling the interest-bearing liability in the separate income statement over the period of such liability.

If a liability is redeemed or settled early, the difference between its amount in the separate statement of financial position and the price of settlement is recorded in the separate income settlement.

Provisions

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

Equity

In accordance with amendments to IAS 32, *Financial Instruments: Presentation,* and IAS 1, *Presentation of Financial Statements – Puttable Financial Instruments and Obligations Arising on Liquidation,* that were issued in February 2008, participants' shares are recognized in equity and not in liabilities.

Fiduciary assets

Assets held in a fiduciary capacity are not reported in the financial statements, as they are not the assets of the Bank.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Recognition of income and expenses

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

Interest and similar income and expense

For all financial instruments measured at amortized cost and interest-bearing securities classified as trading or available-for-sale, interest income or expense is recorded at the effective interest rate, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument (for example, prepayment options) and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the effective interest rate, but not future credit losses. The carrying amount of the financial asset or financial liability is adjusted if the Bank revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest income or expense.

Once the recorded value of a financial asset or a group of similar financial assets has been reduced due to an impairment loss, interest income continues to be recognized using the original effective interest rate applied to the new carrying amount.

Fee and commission income

The Bank earns fee and commission income from a diverse range of services it provides to its customers. Fee income can be divided into the following two categories:

- *Fee income earned from services that are provided over a certain period of time*

Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income and credit and deposit fees. Loan commitment fees for loans that are likely to be drawn down and other credit related fees are deferred (together with any incremental costs) and recognized as an adjustment to the effective interest rate on the loan.

- *Other fee and commission income*

Fees earned for the provision of transaction services are recognized on completion of the underlying transaction. Fees or components of fees that are linked to a certain performance are recognized after fulfilling the corresponding criteria.

Fee and commission expense

Fee and commission expenses comprise commissions on securities transactions and commissions on cash settlement transactions. Commissions paid on purchase of securities classified as financial instruments at fair value through profit or loss are recognized in the separate income statement at the purchase date. Commissions paid on all other purchases of securities are recognized as an adjustment to the carrying amount of the instrument with corresponding adjustment to its effective yield.

Commissions on cash settlement transactions are recorded in the separate income statement at the date when the relevant service is provided.

Dividend income

Income is recognized when the Bank's right to receive the payment is established.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Future changes in accounting policies

Standards and interpretations issued but not yet effective

IFRS 9, Financial Instruments (first phase)

In November 2009 and 2010 the IASB issued the first phase of IFRS 9, *Financial Instruments*. This standard will eventually replace IAS 39, *Financial Instruments: Recognition and Measurement*. IFRS 9 becomes effective for annual periods beginning on or after 1 January 2015. The first phase of IFRS 9 introduces new requirements for classification and measurement of financial assets. In particular, for subsequent measurement all financial assets are to be classified at amortized cost or at fair value through profit or loss with the irrevocable option for equity instruments not held for trading to be measured at fair value through other comprehensive income. There is a new requirement for financial liabilities recognized through profit or loss using a fair value option that the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability shall be presented in other comprehensive income. The Bank now evaluates the impact of the adoption of the new Standard and considers the initial application date.

IFRS 10, Consolidated Financial Statements

IFRS 10, *Consolidated Financial Statements,* establishes a single control model that applies to all entities including special purpose entities. The changes introduced by IFRS 10 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. In addition IFRS 10 introduces specific application guidance for agency relationships. The standard also contains accounting requirements and consolidation procedures, which are carried over unchanged from IAS 27. IFRS 10 replaces the consolidation requirements in SIC-12, *Consolidation – Special Purpose Entities,* and IAS 27, *Consolidated and Separate Financial Statements,* and is effective for annual periods beginning on or after 1 January 2013. Early application is permitted. The Bank expects that the application of IFRS 10 will have no impact on the Bank’s financial position or performance presented in the separate financial statements.

IFRS 11, Joint Arrangements

IFRS 11 removes the option to account for jointly controlled entities using proportionate consolidation. Instead, jointly controlled entities that meet the definition of a joint venture must be accounted for using the equity method. IFRS 11 supersedes IAS 31, *Interests in Joint Ventures,* and SIC-13, *Jointly Controlled Entities – Non-monetary Contributions by Venturers,* and becomes effective for annual reporting periods starting on or after 1 January 2013. Early application is permitted. The Bank expects that these amendments will have no impact on the Bank’s financial position or performance presented in the separate financial statements.

IFRS 12, Disclosure of Interests in Other Entities

IFRS 12 contains all disclosure requirements that were previously included in IAS 27 related to consolidated financial statements, as well as all disclosure requirements that were previously included in IAS 31 and IAS 28. These disclosures relate to an entity’s interests in subsidiaries, joint arrangements, associates and structured entities. A number of new disclosures are also required for such entities. This standard becomes effective for annual reporting periods beginning on or after 1 January 2013. Early application is permitted. Adoption of the standard will require additional disclosures to be made in the financial statements of the Bank but will have no impact on its financial position or performance.

IFRS 13, Fair Value Measurement

IFRS 13 establishes a single source of guidance under IFRS for all fair value measurements. IFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under IFRS when fair value is required or permitted. This standard becomes effective for annual reporting periods beginning on or after 1 January 2013. Early application is permitted. The adoption of IFRS 13 may have effect on the measurement of the Bank’s assets and liabilities accounted for at fair value. The Bank is currently evaluating the possible impact of IFRS 13 on its financial position and performance.

IAS 27, Separate Financial Statements (as revised in 2011)

As a consequence of the new IFRS 10 and IFRS 12, what remains of IAS 27 is limited to accounting for subsidiaries, jointly controlled entities, and associates in separate financial statements. The amendment becomes effective for annual reporting periods beginning on or after 1 January 2013.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Future changes in accounting policies (continued)

IAS 28, Investments in Associates and Joint Ventures (revised 2011)

As a consequence of the new IFRS 11 and IFRS 12, IAS 28 has been renamed IAS 28, *Investments in Associates and Joint Ventures*, and describes the application of the equity method to investments in joint ventures in addition to associates. The amendment becomes effective for annual reporting periods beginning on or after 1 January 2013. The Bank expects that these amendments will have no impact on the Bank’s financial position or performance presented in the separate financial statements.

Amendments to IFRS 7, Financial Instruments: Disclosures

The Amendments were issued in October 2010 by the IASB and are effective for annual reporting periods beginning on or after 1 July 2011. The amendment introduces additional disclosure requirements for transferred financial assets that are not derecognized to enable the user of the Bank’s financial statements to understand the relationship with those assets that have not been derecognized and their associated liabilities. In addition, the amendment requires disclosures about continuing involvement in derecognized assets to enable the users to evaluate the nature of, and risks associated with, the entity’s continuing involvement in those derecognized assets. The amendment affects disclosure only and has no impact on the Bank’s financial position or performance.

Standards and interpretations issued but not yet effective

Amendments to IAS 12, Income Taxes – Deferred tax: Recovery of Underlying Assets

In December 2010 the IASB issued amendments to IAS 12 effective for annual periods beginning on or after 1 January 2012. The amendment clarifies the determination of deferred tax on investment property measured at fair value. The amendment introduces a rebuttable presumption that deferred tax on investment property measured using the fair value model in IAS 40 should be determined on the basis that its carrying amount will be recovered through sale. Furthermore, it introduces the requirement that deferred tax on non-depreciable assets that are measured using the revaluation model in IAS 16 should always be measured on a sale basis. This amendment will have no impact on the Bank's separate financial statements.

Amendment to IAS 19, Employee Benefits

The amendment to IAS 19 becomes effective for annual reporting periods beginning on or after 1 January 2013. The amendment introduces significant changes to the method of accounting for employee benefits, including the removal of the option for deferred recognition of changes in pension plan assets and liabilities (known as the "corridor approach"). In addition, the amendment limits changes in net pension assets (liabilities) recognized in profit and loss to net interest income (expense) and cost of services. The amendment will have no significant impact on the Bank's financial position or performance.

Amendment to IAS 1, Presentation of Financial Statements – Presentation of Other Comprehensive Income

The amendment to IAS 1 becomes effective for annual reporting periods beginning on or after 1 July 2012. The amendment changes the grouping of items presented in other comprehensive income. Items that could be reclassified to profit or loss at a future point in time (for example, upon derecognition or settlement) would be presented separately from items that will never be reclassified. The amendment affects presentation only and will have no impact on the Bank's financial position or performance.

Amendment to IFRS 1, First-time Adoption of International Financial Reporting Standards – Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters

The amendment becomes effective for annual reporting periods beginning on or after 1 July 2011. The amendment introduces a new deemed cost exemption for entities that have been subject to severe hyperinflation. The amendment will have no impact on the Bank's financial position or performance.

(Thousands of Euros)

4. Significant accounting judgments and estimates

Assumptions and estimation uncertainty

Management made a number of estimates and assumptions, which affect the separate reporting of assets and liabilities and the carrying value of assets and liabilities in the next financial year. Estimates and assumptions are continuously assessed and are based on the management experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. In addition, management relies on judgments and assessments in applying the accounting policies.

Most significant judgments which affect the amounts recorded in the separate financial statements, and estimates which may result in significant adjustment of the carrying value of assets and liabilities in the next financial year are presented below:

Allowance for loan impairment

The Bank regularly reviews its loans to assess impairment. In determining whether an impairment loss should be recorded in the separate income statement, the Bank makes judgments as to whether there is any objective evidence indicating that there is a measurable decrease in the estimated future cash flows from a loan. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers or national or local economic conditions that correlate with defaults on liabilities. Impairment loss may be reversed only if a subsequent increase can be objectively related to an event occurring after the impairment loss was recognized. For uncollectible debt, the Bank makes allowance in the amount equal to 100% of the amount of debt. Loans are written off at the decision of the Council of the Bank when no economic benefits are expected from them. Loans are recorded in the Bank's separate statement of financial position less allowances for impairment.

Fair values of financial instruments

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by the market price. The estimated fair values of financial instruments have been determined by the Bank using available market information, where it exists, and appropriate valuation methodologies. However, judgment is necessarily required to interpret market data to determine the estimated fair value. The fair value of derivative financial instruments that are not quoted in an active market is determined using valuation methodologies. To the extent it is applicable, the models use only available market information, but certain areas require management estimates. Change in the assessment of these factors may affect fair value reflected in the financial statements. Management has used all available market information in estimating the fair value of financial instruments.

Fair values of buildings and investment property

As disclosed in Note 3, starting from 31 December 2010 the Bank changed its accounting policy with regard to buildings and investment property. The historical cost model was replaced by the fair value model.

As for buildings, the Bank monitors the compliance of the value of buildings with their fair value and performs revaluation to ensure that the present value of buildings does not differ materially from their fair value. The date of the latest revaluation of the Bank's buildings was 26 December 2011. Starting from 26 December 2011, the revalued building is depreciated in accordance with the remaining useful life. Changes in the fair value are recognized in other comprehensive income. For evaluating purposes the Bank engages independent professional appraisers and applies an appropriate valuation methodology and information on transactions with similar real estate objects on the local market. However, valuation results based on the above valuation method may differ from the prices of actual transactions on the real estate market.

As for investment property, the Bank monitors changes in its fair value at each reporting date to ensure that the current value of investment property does not differ materially from its fair value. The date of the latest revaluation of the Bank's investment property was 26 December 2011. At 31 December 2011, there were no significant changes in the fair value. Changes in the fair value of investment property are recognized in the separate income statement. The Bank determines the fair value of investment property by engaging independent professional appraisers and applying an appropriate valuation methodology and information on transactions with similar real estate objects on the local market. However, valuation results based on the above valuation method may differ from the prices of actual transactions on the real estate market.

Impairment of equity securities available for sale

The Bank determines that available-for-sale equity investment securities are impaired when there has been a significant or prolonged decline in the fair value below their cost. The determination of what is significant or prolonged requires judgment. In making this judgment, the Bank evaluates, among other factors, the volatility of share prices. In addition, impairment may take place when there is evidence of a deterioration in the financial health of the investee, industry and sector performance, changes in technology, and operating or financing cash flows.

(Thousands of Euros)

4. Significant accounting judgments and estimates (continued)

Assumptions and estimation uncertainty (continued)

In particular, information on significant areas of estimation uncertainty and critical judgments in applying accounting policies is presented in the following notes:

- Note 8: Financial instruments at fair value through profit or loss
- Note 9: Available-for-sale investment securities
- Note 10: Held-to-maturity investment securities
- Note 11: Loans to customers
- Note 13: Investment property
- Note 14: Property and equipment
- Note 18: Contingencies and lending commitments

5. Restatement of comparative information

In accordance with the accounting policy applied by the Bank, cash and cash equivalents include cash on hand, accounts with banks and other financial institutions which mature within ninety days from the origination date and are free from contractual encumbrances. But until 2011 the Bank consistently classified short-term deposits maturing within 90 days and placed with reliable counterparties having high credit ratings as deposits with banks and other financial institutions.

The Bank recognized coupon income from combined financial instruments for 2010 in the amount of EUR 2,301 thousand as net non-interest income in its financial statements as of 31 December 2010. However, in accordance with the Bank's accounting policy interest income from financial instruments at fair value through profit or loss shall be recorded as interest income.

The previously issued separate financial statements as of 31 December 2010 and for the year then ended were adjusted during the preparation of the Bank's separate financial statements as of 31 December 2011 and for the year then ended. The independent auditors' report based on the results of the audit of 2010 financial statements was issued on 15 March 2011. The effect of this restatement on the financial statement items as of 31 December 2010 and 31 December 2009 is presented below.

	As previously reported	*Effect of adjustment*	*As restated*
Separate statement of financial position as of 31 December 2010			
Cash and cash equivalents	2,529	87,194	89,723
Deposits with banks and other financial institutions	117,246	(87,194)	30,052
Separate income statement for the year ended 31 December 2010			
Interest income	8,256	2,301	10,557
Net interest income	**8,247**	**2,301**	**10,548**
Net interest loss after allowance for loan impairment	**(7,146)**	**2,301**	**(4,845)**
Net gains/(losses) from financial instruments at fair value through profit or loss			
- *Coupon income from combined financial instruments*	2,301	(2,301)	–
Net non-interest income	**43,346**	**(2,301)**	**41,045**
Separate statement of financial position as of 31 December 2009			
Cash and cash equivalents	7,394	92,214	99,608
Deposits with banks and other financial institutions	132,277	(92,214)	40,063
Separate statement of cash flows for the year ended 31 December 2010			
Cash flows from operating activities			
Net (increase)/decrease in operating assets			
Deposits with banks and other financial institutions	15,131	(5,020)	10,111
Net cash flows from operating activities	**27,206**	**(5,020)**	**22,186**
Net (decrease)/increase in cash and cash equivalents	**(4,865)**	**(5,020)**	**(9,885)**
Cash and cash equivalents, beginning	**7,394**	**92,214**	**99,608**
Cash and cash equivalents, ending	**2,529**	**87,194**	**89,723**

The effect of the above changes is also disclosed in Notes 6, 7 and 21.

(Thousands of Euros)

6. Cash and cash equivalents

Cash and cash equivalents comprise:

	2011	*2010 (restated)*	*2009 (restated)*
Cash on hand	**29**	**177**	**58**
Nostro accounts with banks and other financial institutions			
Credit rating AAA	449	1,802	6,165
Credit rating AA-	–	–	1
Credit rating from A- to A+	317	314	386
Credit rating from BBB- to BBB+	11	232	781
No credit rating	4	4	3
Total Nostro accounts with banks and other financial institutions	**781**	**2,352**	**7,336**
Short-term deposits with banks			
Term deposits with banks			
Credit rating from AA- to AA+	–	–	12,004
Credit rating from A- to A+	9,503	77,055	68,034
Credit rating from BBB- to BBB+	565	6,000	2,086
	10,068	**83,055**	**82,124**
Reverse repurchase agreements – *No credit rating*	3,023	4,139	10,090
Total short-term deposits with banks	**13,091**	**87,194**	**92,214**
Cash and cash equivalents	**13,901**	**89,723**	**99,608**

Cash and cash equivalents are neither impaired, nor past due.

As at 31 December 2011, the Bank had no counterparties (2010 – no counterparties) whose balances on nostro accounts exceeded 10% of the Bank's equity.

As at 31 December 2011, the Bank had no counterparties (2010 – no counterparties) whose balances on short-term deposit accounts exceeded 10% of the Bank's equity.

As at 31 December 2011 and 31 December 2010, the Bank entered into reverse repurchase agreements with the Central Cooperative Bank, Sophia. The subject of these agreements was investment-rated sovereign Bulgarian Eurobonds. As at 31 December 2011, the fair value of the Eurobonds was EUR 3,358 thousand (2010 – EUR 4,864 thousand). As at 31 December 2009, the Bank entered into reverse repurchase agreements with Ronin Europe Ltd. The subject of these agreements was investment-rated Eurobonds issued by Russian companies. As at 31 December 2009, the fair value of the Eurobonds was EUR 11,900 thousand.

7. Deposits with banks and other financial institutions

Deposits with banks and other financial institutions comprise:

	2011	*2010 (restated)*	*2009 (restated)*
Term deposits with banks:			
Credit rating from A- to A+	71,146	20,027	30,022
Credit rating from BBB- to BBB+	40,098	–	–
No credit rating	–	10,025	–
Total term deposits with banks	**111,244**	**30,052**	**30,022**
Security deposits on transactions with combined financial instruments			
Credit rating from A- to A+	–	–	10,041
Total security deposits on transactions with combined financial instruments	**–**	**–**	**10,041**
Deposits with banks and other financial institutions	**111,244**	**30,052**	**40,063**

(Thousands of Euros)

7. Deposits with banks and other financial institutions (continued)

Security deposits on transactions with combined financial instruments represented deposits with major international banks that issued first-to-default credit linked notes (hereinafter the "banks issuing first-to-default credit linked notes") (Note 8). As at 31 December 2009, the security deposit amounted to EUR 10,000 thousand at par. As at 31 December 2009, the maximum amount that the Bank was contractually bound to deposit with the banks issuing first-to-default credit linked notes was EUR 10,000 thousand at par.

As at 31 December 2011, deposits with banks in the Republic of Cuba made before 1990 amounted to EUR 35,049 thousand (2010 – EUR 34,774 thousand). These balances accounted for over 10% of the total deposits with banks and other financial institutions. The Bank made a 100% allowance for impairment of these deposits. As at 31 December 2011, the abovementioned allowance amounted to EUR 35,049 thousand (2010: EUR 34,774 thousand).

Republic of Cuba	***2011***	***2010***
Term deposits with banks		
No credit rating	35,049	34,774
	35,049	**34,774**
Less: allowance for impairment	(35,049)	(34,774)
Deposits with banks and other financial institutions	–	–

Information on change in the allowance for impairment of deposits with banks in the Republic of Cuba:

	2011	***2010***
At 1 January	**34,774**	**33,255**
Change in allowance resulting from changes in exchange rates	275	1,519
At 31 December	**35,049**	**34,774**

Repayment of the deposits with banks in the Republic of Cuba is a lasting process and the management believes that these receivables are deposits only formally and historically and are not relevant to the actual state of the Bank's deposits. As a result, the Bank does not include this debt (for which there is a 100% allowance) in the calculation of the quality and concentration of the Bank's deposits.

Concentration of deposits with banks and other financial institutions

As at 31 December 2011, the Bank had no counterparties (2010 – no counterparties) accounting for over 10% of the Bank's total deposits with banks and other financial institutions.

8. Financial instruments at fair value through profit or loss

The Bank accounted for combined instruments represented by a quoted first-to-default credit linked note and a collaterised debt obligation.

As at 31 December 2010, the quoted first-to-default credit linked note was represented by a Euro-denominated note with a total par value of EUR 10,000 thousand (2010 – EUR 10,000 thousand) issued by JP Morgan Chase Bank, N. A. London branch, and bearing interest at a fixed coupon rate of 16%. As at 31 December 2010, fair value of this instrument amounted to EUR 10,496 thousand.

As at 31 December 2010, the collaterised debt obligation was represented by a Euro-denominated note with a total par value of EUR 7,500 thousand issued by Salisbury International Investment Ltd and bearing interest at a floating coupon rate of 3-month LIBOR plus 10%. As at 31 December 2010, fair value of this instrument amounted to EUR 5,236 thousand.

(Thousands of Euros)

9. Available-for-sale investment securities

Available-for-sale investment securities comprise:

	2011	*2010*
Quoted debt securities		
Government bonds of member countries and municipal bonds:		
Eurobonds issued by governments of member countries	22,745	24,225
Bonds of local governments and municipal bonds	10,217	5,447
Government bonds of member countries and municipal bonds	**32,962**	**29,672**
Corporate bonds:		
Credit rating from A- to A+	–	2,134
Credit rating from BBB- to BBB+	34,759	19,155
Credit rating from BB- to BB+	1,115	2,122
Corporate bonds	**35,874**	**23,411**
Foreign government bonds	–	5,725
Total quoted debt securities	**68,836**	**58,808**
Quoted equity instruments		
Credit rating from BB- to BB+	2,199	3,374
Total quoted equity instruments	**2,199**	**3,374**
Available-for-sale investment securities	**71,035**	**62,182**

Government bonds of member countries represent EUR-denominated securities issued and guaranteed by the Ministries of Finance of these countries, maturing in 2013-2025 (2010 – maturing in 2013-2025). The annual coupon rate for these bonds varies from 3.8% to 7.5% (2010 – from 2.3% to 7.5%).

Bonds of local governments and municipal bonds represent EUR-denominated and RUR-denominated bonds issued by the cities of Moscow and Saint-Petersburg, maturing in 2015-2016 (2010 – maturing in 2016). The annual coupon rate for these bonds varies from 5.1% to 7.8% (2010 – 5.1%).

Corporate bonds are represented by the bonds issued by major companies and banks of member countries and EU countries, maturing in 2011-2017 (2010 – maturing in 2011-2020). The annual coupon rate for these bonds varies from 4.5% to 10.81% (2010 – from 5.1% to 8.5%).

Quoted equity securities are represented by shares of a major Russian company.

10. Held-to-maturity investment securities

As at 31 December 2011, held-to-maturity investment securities include quoted Eurobonds of Rosbank International Finance B.V. with the carrying amount of EUR 423 thousand (2010 – EUR 407 thousand).

11. Loans to customers

The Bank issued loans to customers operating in the following countries:

	2011	*2010*
Russian Federation	99,659	110,911
Mongolia	19,225	17,963
Republic of Bulgaria	2,930	2,880
Slovak Republic	3,876	1,001
Total loans to customers	**125,690**	**132,755**
Less: allowance for loan impairment	(74,731)	(77,703)
Loans to customers	**50,959**	**55,052**

(Thousands of Euros)

11. Loans to customers (continued)

	2011	*2010*
Republic of Cuba	45,173	44,043
Total loans to customers	**45,173**	**44,043**
Less: allowance for loan impairment	(45,173)	(44,043)
Loans to customers	**–**	**–**

Loans to borrowers in the Republic of Cuba originated during the period 1985-1990. As at 31 December 2011, total receivables relating to these loans amount to EUR 45,173 thousand (2010 – EUR 44,043 thousand). In December 1990, the Republic of Cuba discontinued payments to repay the debt. Due to the absence of collateral, delays for years and difficult economic conditions in Cuba, the Bank made a 100% allowance for the debt in the amount of EUR 45,173 thousand as at 31 December 2011 (2010 – EUR 44,043 thousand).

Repayment of the loans issued to borrowers in the Republic of Cuba is a lasting process and the management believes that these receivables relate to the Bank’s loan portfolio just formally and historically and are not relevant to the actual state of the Bank’s loan portfolio. In view of the above, receivables relating to borrowers in the Republic of Cuba, for which a 100% allowance was made, are neither included in the calculation of the quality of the Bank's loan portfolio nor reflected in the tables below.

Overdue loans

A summary of overdue loans as at 31 December 2011 and 2010 is presented below:

	2011	*2010*
Total loans for which the principal and/or interest is overdue	91,226	90,630
Total loans to customers	**91,226**	**90,630**
Less: allowance for loan impairment	(71,869)	(75,290)
Loans to customers	**19,357**	**15,340**

Allowance for loan impairment has been allocated to loans as follows:

	Russian Federation	*Mongolia*	*Republic of Bulgaria*	*Total*
At 1 January 2011	**72,283**	**5,412**	**8**	**77,703**
Net charge for the year	3,772	82	(8)	**3,846**
Amounts written off	(7,004)	–	–	**(7,004)**
Change in allowance resulting from changes in exchange rates	154	32	–	**186**
At 31 December 2011	**69,205**	**5,526**	**–**	**74,731**
Individual impairment	**69,205**	**5,526**	**–**	**74,731**
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	**99,659**	**11,911**	**2,930**	**114,500**

	Russian Federation	*Mongolia*	*Republic of Bulgaria*	*Total*
At 1 January 2010	**53,558**	**5,760**	**2,614**	**61,932**
Net charge for the year	18,412	(413)	(2,606)	**15,393**
Change in allowance resulting from changes in exchange rates	313	65	–	**378**
At 31 December 2010	**72,283**	**5,412**	**8**	**77,703**
Individual impairment	**72,283**	**5,412**	**8**	**77,703**
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	**110,911**	**11,963**	**2,880**	**125,754**

(Thousands of Euros)

11. Loans to customers (continued)

Overdue loans (continued)

As at 31 December 2011 and 2010 there were no overdue but not impaired loans in the Bank's portfolio.

Change in these estimates may influence the size of allowance for loan impairment. For example, if the net present value of estimated future cash flows has increased/declined by 1%, allowance for impairment would have declined/increased by EUR 510 thousand as at 31 December 2011 (2010 – by EUR 551 thousand).

Concentration of loans to customers

As at 31 December 2011, loans to three borrowers (2010 – three) with the total amount of loans to each of the three borrowers exceeding 10% of total loans to customers were recorded on the Bank's balance sheet. As at 31 December 2011, these loans total comprised EUR 54,749 thousand (2010 – EUR 54,315 thousand) and an allowance of EUR 32,778 thousand (2010 – EUR 24,332 thousand) has been made for them.

Analysis of collateral

The following table provides an analysis of the loan portfolio, net of allowance for impairment, by types of collateral as at 31 December 2011 and 2010:

	2011		*2010*	
	Loans net of allowance for impairment	*Share in the total loans, %*	*Loans net of allowance for impairment*	*Share in the total loans, %*
Pledge of real property (mortgage) and title	31,130	61.0	23,162	42.1
Pledge of equipment and goods in turnover	16,895	33.2	28,423	51.6
Pledge of rights of demand and construction	405	0.8	3,153	5.7
Other	306	0.6	314	0.6
Total	**48,736**	**95.6**	**55,052**	**100.0**

The amounts shown in the table above represent the carrying value of the loan portfolio, and do not necessarily represent the fair value of the collateral.

As at 31 December 2011, fair value of collateral based on which impaired loans are provided for, amounted to EUR 29,378 thousand (2010 – EUR 15,623 thousand).

Analysis of loans by industry

The Bank issued loans to borrowers operating in the following industries:

	2011	*2010*
Construction of buildings	39,412	45,421
Production, transmission and distribution of electricity, gas and steam	32,551	32,117
Food and beverage	25,191	25,907
Mining	12,340	12,949
Timber manufacturing	10,005	10,005
Specialized construction	3,876	3,471
Rubber and plastic manufacturing	1,368	1,319
Air transport	947	915
Leather manufacturing	–	651
	125,690	**132,755**
Less: allowance for loan impairment	(74,731)	(77,703)
Loans to customers	**50,959**	**55,052**

(Thousands of Euros)

12. Assets held for sale

Assets held for sale are represented by collateral received by the Bank from its debtors who failed to fulfill their obligations on the settlement of overdue loans. The Bank plans to realize these assets within 12 months and takes active actions for their further sale. Management believes that the assets received can be qualified as assets held for sale. As at 31 December 2011, assets held for sale comprise real estate and property rights to equity construction objects.

Property rights to participatory construction objects	1,719
Real estate	329
Assets held for sale	**2,048**

13. Investment property

In 2011 and 2010, the following changes occurred in the cost of property under operating lease:

	2011	*2010*
Cost		
At 1 January	**47,951**	**25,089**
Additions	581	674
Accounting for accumulated depreciation at revaluation	–	(9,386)
Transfers	–	2,592
Effect of revaluation	1,755	28,982
At 31 December	**50,287**	**47,951**
Depreciation		
At 1 January	**–**	**(9,422)**
Depreciation charge	–	(545)
Disposals	–	–
Accounting for accumulated depreciation at revaluation	–	9,386
Transfers	–	581
At 31 December	**–**	**–**
Net book value as at 31 December	**50,287**	**47,951**

The Bank rents buildings under operating lease agreements. In 2011, the Bank's income from lease of investment property amounted to EUR 6,763 thousand (2010 – EUR 6,153 thousand).

The Bank engaged an independent appraiser to determine the fair value of its buildings. The valuation services were performed by an independent firm of professional appraisers which have acknowledged qualification and relevant professional experience in appraising real property of a similar category and in a similar location. Fair value is determined by reference to market-based evidence. The date of the revaluation was 26 December 2011. If the investment property was measured using the cost model, the carrying amounts as of 31 December 2011 would be as follows:

	2011	*2010*
Cost	28,791	28,355
Accumulated depreciation	(10,004)	(9,433)
Net book value	**18,787**	**18,922**

(Thousands of Euros)

14. Property and equipment

The movements in property and equipment for the year ended 31 December 2011 were as follows:

	Buildings	*Equipment*	*Computers and software*	*Office furniture*	*Vehicles*	*Total*
Cost						
At 1 January 2011	**46,070**	**7,688**	**2,700**	**502**	**553**	**57,513**
Additions	559	538	556	–	2	**1,655**
Disposals	–	(213)	–	(6)	–	**(219)**
Accounting for accumulated depreciation at revaluation	(1,560)	–	–	–	–	**(1,560)**
Transfers	–	–	–	–	–	**–**
Effect of revaluation	3,246	–	–	–	–	**3,246**
At 31 December 2011	**48,315**	**8,013**	**3,256**	**496**	**555**	**60,635**
Accumulated depreciation						
At 1 January 2011	**(120)**	**(7,233)**	**(1,864)**	**(340)**	**(444)**	**(10,001)**
Depreciation charge	(1,440)	(265)	(674)	(20)	(72)	**(2,471)**
Disposals	–	212	–	5	–	**217**
Transfers	–	–	–	–	–	**–**
Accounting for accumulated depreciation at revaluation	1,560	–	–	–	–	**1,560**
At 31 December 2011	**–**	**(7,286)**	**(2,538)**	**(355)**	**(516)**	**(10,695)**
Net book value						
At 31 December 2010	**45,950**	**455**	**836**	**162**	**109**	**47,512**
At 31 December 2011	**48,315**	**727**	**718**	**141**	**39**	**49,940**

The movements in property and equipment for the year ended 31 December 2010 were as follows:

	Buildings	*Equipment*	*Computers and software*	*Office furniture*	*Vehicles*	*Total*
Cost						
At 1 January 2010	**31,845**	**4,977**	**2,121**	**551**	**592**	**40,086**
Additions	583	118	579	6	–	**1,286**
Disposals	–	–	–	(55)	(39)	**(94)**
Accounting for accumulated depreciation at revaluation	(9,018)	–	–	–	–	**(9,018)**
Transfers	(5,185)	2,593	–	–	–	**(2,592)**
Effect of revaluation	27,845	–	–	–	–	**27,845**
At 31 December 2010	**46,070**	**7,688**	**2,700**	**502**	**553**	**57,513**
Accumulated depreciation						
At 1 January 2010	**(10,332)**	**(4,602)**	**(1,291)**	**(372)**	**(384)**	**(16,981)**
Depreciation charge	(707)	(149)	(573)	(23)	(99)	**(1,551)**
Disposals	–	–	–	55	39	**94**
Transfers	1,901	(2,482)	–	–	–	**(581)**
Accounting for accumulated depreciation at revaluation	9,018	–	–	–	–	**9,018**
At 31 December 2010	**(120)**	**(7,233)**	**(1,864)**	**(340)**	**(444)**	**(10,001)**
Net book value						
At 31 December 2009	**21,513**	**375**	**830**	**179**	**208**	**23,105**
At 31 December 2010	**45,950**	**455**	**836**	**162**	**109**	**47,512**

As at 31 December 2011, the cost of fully depreciated property and equipment still used by the Bank was EUR 7,064 thousand (2010 – EUR 7,295 thousand).

The Bank engaged an independent appraiser to determine the fair value of its buildings. The valuation services were performed by an independent firm of professional appraisers which have acknowledged qualification and relevant professional experience in appraising real property of a similar category and in a similar location. Fair value is determined by reference to market-based evidence.

(Thousands of Euros)

14. Property and equipment (continued)

The date of the revaluation was 26 December 2011. If the buildings were measured using the cost model, the carrying amounts as of 31 December 2011 would be as follows:

	2011	*2010*
Cost	27,801	27,243
Accumulated depreciation	(9,612)	(9,063)
Net book value	**18,189**	**18,180**

15. Other assets and liabilities

Other assets comprise:

	2011	*2010*
Advance payments	1,565	1,809
Other accounts receivable	6	462
	1,571	**2,271**
Less: provision for impairment of other assets	(119)	(133)
Other assets	**1,451**	**2,138**

Other liabilities comprise:

	2011	*2010*
Other accounts payable	3,210	3,854
Provision for potential VAT payments related to income from leases	1,895	1,927
Settlements with employees	544	475
Other	124	120
Other liabilities	**5,773**	**6,376**

16. Due to banks and other financial institutions

Due to banks and other financial institutions comprise:

	2011	*2010*
Correspondent accounts of banks	1	982
Due to banks and other financial institutions	**1**	**982**

17. Equity

Equity

The Bank's subscribed capital amounts to EUR 1,300,000 thousand which represents the Bank's equity stated in the Agreement. The Bank's member countries make contributions to the Bank's equity pursuant to their shares stipulated in the Agreement. Callable capital is the amount of contributions by the Bank's member countries which have not been made yet.

(Thousands of Euros)

17. Equity (continued)

Revaluation reserve for available-for-sale investment securities and revaluation reserve for property and equipment

The movements in the revaluation reserve for available-for-sale investment securities and revaluation reserve for property and equipment were as follows:

	Revaluation reserve for available-for-sale investment securities	*Revaluation reserve for property and equipment*
At 1 January 2010	**3,951**	**–**
Net unrealized losses on available-for-sale investment securities	(384)	–
Realized gains on available-for-sale investment securities reclassified to the income statement	(3,014)	–
Revaluation of buildings	–	27,845
At 31 December 2010	**553**	**27,845**
Net unrealized losses on available-for-sale investment securities	(2,476)	–
Realized gains on available-for-sale investment securities reclassified to the income statement	(428)	–
Revaluation of buildings	–	3,246
At 31 December 2011	**(2,351)**	**31,091**

Revaluation reserve for available-for-sale investment securities

This reserve records fair value changes of available-for-sale investments.

Revaluation reserve for property and equipment

The revaluation reserve for property and equipment is used to record increases in the fair value of buildings and decreases to the extent that such decrease relates to an increase on the same asset previously recognized in other comprehensive income.

18. Contingencies and loan commitments

Legal

In accordance with the Agreement on the establishment of the Bank, its assets (irrespective of their location) enjoy immunities from any administrative and legal claims.

In the ordinary course of business, the Bank acts as a plaintiff in a number of court proceedings against its borrowers. The Bank takes all necessary legal and other actions to collect the bad debt and to realize respective repossession rights. When the estimated amount of costs resulting from the Bank's further actions to collect bad debt and/or realize respective repossession rights is higher than the amount collected and also when the Bank holds necessary and sufficient documents and/or regulations issued by the governmental authorities, it decides to write off such bad debt against the respective provision.

Insurance

The Bank obtained insurance coverage for a group of buildings, equipment and car park as well as liability insurance against damages caused by operating assets of a hazardous nature. However, the Bank did not obtain insurance coverage related to temporarily discontinued operations or the Bank's obligations to third parties.

(Thousands of Euros)

18. Contingencies and loan commitments (continued)

Commitments and contingencies

At any time the Bank has outstanding commitments to extend loans. These commitments take the form of approved loan agreements.

The contractual amounts of off-balance sheet commitments are set out in the table below. The amounts reflected in the table for commitments assume that amounts are fully advanced.

On 31 December, the Bank's financial commitments and contingencies comprised the following:

	2011	*2010*
Credit related commitments		
Undrawn loan facilities	24,139	11,545
Commitments and contingencies	**24,139**	**11,545**

19. Leases

Bank as lessor

The Bank provides its real estate for operating leases. The Bank's non-cancelable operating lease rentals are receivable as follows:

	2011	*2010*
Less than 1 year	5,131	4,360
Leases	**5,131**	**4,360**

20. Loan and deposit trust operations

Loan and deposit operations are one of the types of agency/trust operations that imply the agent carrying certain actions in its own name; however, all expenses and risks are borne by the client whose name is not disclosed. Loan and deposit operations involve the following parties:

"Bank" is a bank which (for the purpose of a loan and deposit operation) acts as the Client's agent to provide a credit related product to a Third Party on the Client's behalf, at the Client's expense and on terms determined by the Client.

"Client" is the Bank's customer requesting to carry out a loan and deposit operation and providing guaranty (coverage, security deposit). Such guaranty limits the amount of a credit related product provided by the Bank to a Third Party by setting risk-free terms.

"Third Party" is a recipient of the Bank's credit related product determined by the Client.

The Bank performs such operations considering the reputational risk and the fact that the Client accepts all risks.

The Bank records such operations as a transfer of financial assets as the Bank retains contractual claims to receive cash flows from financial assets ("original asset"), but commits to transfer these cash flows to one or more entities ("eventual recipients") on the following conditions:

- The Bank shall pay cash to eventual recipients upon receipt of equivalent amounts from the original asset;
- Pursuant to the transfer agreement, the Bank may not sell or pledge original asset for any purpose except guarantying its obligation to pay cash flows to the eventual recipients;
- The Bank has no significant delays in transfers of any cash flows received on behalf of the eventual recipients. In addition, the Bank may not reinvest such cash flows (except investment in form of cash or cash equivalents) within a short period from the day of their receipt to the day of required transfer to eventual recipients. Interest income from such investment shall be transferred to eventual recipients.

(Thousands of Euros)

20. Loan and deposit trust operations (continued)

The Bank receives fee income for providing these services.

As at 31 December 2011, the Bank had no funds for loan and deposit trust operations (2010 – EUR 23,414 thousand). Net gains from such operations for the year ended 31 December 2011 amounted to EUR 98 thousand (2010 – EUR 238 thousand).

21. Interest income and interest expense

Net interest income comprises:

	2011	*2010 (restated)*
Loans to customers	3,264	5,632
Available-for-sale investment securities and held-to-maturity investment securities	2,866	1,865
Deposits with banks and other financial institutions	1,678	759
	7,808	**8,256**
Combined financial instruments	757	2,301
Interest income	**8,565**	**10,557**
Due to banks and other financial institutions	(34)	–
Current customer accounts	(21)	(9)
Interest expenses	**(55)**	**(9)**
Net interest income	**8,510**	**10,548**

As at 31 December 2011, interest income accrued on impaired loans to customers amounted to EUR 2,348 thousand (2010 – EUR 4,902 thousand).

22. Net gain/(loss) from foreign currencies

Net gains less losses from foreign currencies comprise:

	2011	*2010*
Net (loss)/gain from revaluation of assets and liabilities in foreign currencies	(166)	882
Net gain/(loss) from trading	15	(28)
Net (loss)/gain from foreign currencies	**(151)**	**854**

23. General and administrative expenses

General and administrative expenses comprise:

	2011	*2010*
Employee compensations and employment taxes	7,121	6,872
Administration and management	2,839	3,052
Depreciation charge	2,471	2,096
Other	434	424
General and administrative expenses	**12,865**	**12,444**

(Thousands of Euros)

24. Risk management

The Bank classifies risks inherent in its various activities into three main groups:

- financial risks;
- operational risks;
- business risks.

Risk management framework

The Bank’s risk management policy is based on the conservative assessments and is mainly aimed at mitigation of adverse impact of risks on the Bank’s results, i.e. on the safety and reliability of fund allocation while maintaining the reasonable level of profitability. The conservative assessment assumes that the Bank does not enter into potential transactions with high or undeterminable risk level, regardless of profitability.

The Bank's risk management activities are intended to:

- identify, analyze and manage risks faced by the Bank;
- establish ratios and limits that restrict level of the appropriate types of risks;
- monitor the level of the risk and its compliance with established limits;
- develop and implement regulative and methodological documents as well as software applications that ensure the professional risk management for the bank transactions.

Risk management policies and procedures are reviewed regularly to reflect changing situation on the financial markets.

Risk management system

For the purposes of risk management, the Bank applies risk management system which ensures cooperation in the area of risk management among all management bodies, business units and committees of the Bank in accordance with the existing regulatory documents. The main components of the risk management system include the Council, the Audit Committee, the Board, the Asset, Liability and Risk Committee (ALRCO), the Credit Committee and the Risk Management Department.

The Council is the supreme management body of the Bank responsible for its overall management, approval of the Main Risk Management Principles as well as approval of its key risk ratios.

The Audit Committee appointed by the Council audits the Bank’s operations considering all the risk factors stipulated by the Regulation on the Audit Committee of the Bank.

The Board is the executive body of the Bank, which is responsible for compliance with risk management policies and procedures as well as ratios and limits established by the Council. The Board ensures co-operation among all business units and committees of the Bank with regard to risk management.

ALRCO is the Management Board's collegial body responsible for development and implementation of the risk management policy in the course of interbank and security transactions.

The Credit Committee is the Management Board's collegial body responsible for lending and assessment of risks arising from loans, guarantees and other types of credit-related transactions.

Committees meet on a regularly basis and provide to the Management Board their recommendations to improve risk management policies and procedures as well as information on significant transactions.

The Risk Management Department collects and analyzes information related to all types of bank risks, performs their qualitative and quantitative assessment, prepares recommendations for the Management Board and committees of the Bank to mitigate risk impact on the Bank’s performance.

Risk identification

The Bank identifies and manages both external and internal risk factors throughout its organizational structure. As a result of regular analysis of the Bank’s exposure to different types of risks performed by the Risk Management Department, the Bank identifies factors leading to the increase of the risk level and determines the level of assurance over the current risk mitigation procedures. Apart from the standard credit and market risk analysis, the Risk Management Department monitors financial and non-financial risks influencing the results of banking transactions. Current risks exposures and their projected changes are discussed during the meetings of ALRCO and also communicated to the Management Board along with the recommendations on possible risk mitigation measures.

(Thousands of Euros)

24. Risk management (continued)

Risk assessment, management and control

The Bank's risk assessment, reporting and control procedures vary by risk type, but are based on a common methodology developed and updated by the Risk Management Department.

Credit risk

Credit risk is the risk that the Bank will incur a loss because its counterparty fails to discharge its contractual financial obligations to the Bank, or discharged them in an untimely fashion or not in full. Credit risk arises principally from loans and advances to customers and other banks and other on and off balance sheet credit exposures. For risk reporting purposes, the Bank considers and consolidates all elements of credit risk exposures such as individual borrower or counterparty default risk, geographical and industry risk.

For risk management purposes, credit risk arising from financial instruments at fair value through profit or loss is managed and reported as a market risk exposure.

System of credit risk management

Upon preparation of a transaction by the initiating unit it is approved by the Credit Committee, and then – the Management Board. The Management Board is responsible for all direct credit risk exposures up to EUR 10,000 thousand and up to 7 years. Direct credit risks exposures of over EUR 10,000 thousand or above 7 years should be approved by the Council of the Bank.

The objective of credit risk management is to decrease its possible adverse effect on the Bank's performance based on the maintenance of potential losses resulted from credit risk within established limits.

To mitigate credit risk, the Bank limits concentrations of exposure to individual customers, counterparties and issuers (for securities), groups of related customers, counterparties and issuers as well as by industry/sector, credit rating (for securities). Credit risk management process is based on regular analysis of the creditworthiness the borrowers and their ability to repay interest and principal of debt, and on correspondent limits modification (if necessary).

The Bank's regulatory documents establish the following:

- procedures to review and approve loan/credit applications;
- methodology for the credit assessment of borrowers, counterparties, issuers and insurance companies;
- valuation approaches with regard to collateral offered;
- requirements to the credit documentation;
- procedures for the ongoing monitoring of loans and other credit exposures.

The corporate loan/credit application and appropriate project documents are reviewed by the Credit Department. In case of a positive decision, the set of documents from the Credit Department required for reviewing the loan/credit application shall be analyzed by the Legal Department, Risk Management Department, Security Department, Strategic Planning and Analysis Department, and Internal Control and Compliance Department. For the purpose of comprehensive analysis of the loan/credit application received from the Credit Department, the Legal Department and Risk Management Department jointly prepare Description of the Investment Transaction. The loan/credit application is subject to review by the Credit Committee based on the Description of the Investment Transaction, report of the Security Department and Strategic Planning and Analysis Department, report on risks of the Risk Management Department and compulsory judgment of the Legal Department in respect of the legal compliance of the proposed transaction. The procedure of making lending decisions comprises the following steps: Step 1 includes reviewing application by the Credit Committee; Step 2 includes making decision by the Management Board of the Bank (if such issue falls within its competence); Step 3 includes sending a set of respective documents approved by the Management Board of the Bank to the member countries in order to obtain the final approval from the country of origin of the borrower; Step 4 includes making decision by the Council of the Bank (if such issue falls within its competence).

Apart from individual customer analysis, the Risk Management Department assesses the whole loan portfolio with regard to credit concentration and market risks. Based on the Bank's internal rating model to determine borrower's default probability and recovery estimates, the Bank classifies all loans and other credit related products by the respective groups of risks.

(Thousands of Euros)

24. Risk management (continued)

Credit risk (continued)

The Bank continuously monitors the quality of individual credit exposures and regularly reassesses the creditworthiness of its customers. The revaluation is based on the customer's most recent financial statements, past-due status, performance of its business plan and other information submitted by the borrower, or otherwise obtained by the Bank. Based on this information, the borrower's internal credit rating (class of the loan) may be revised and, accordingly, the appropriate loan impairment provision may be created or changed.

Collateral and other credit enhancements

Credit risk is also managed by obtaining pledge of real estate, assets and securities, and other collateral, including corporate and personal guarantees, as well as monitoring availability and value of collateral.

As availability of collateral is important to mitigate credit risk, this factor is a priority for the Bank when reviewing loan/credit applications if their terms and conditions are similar. To ensure recovery of its resources associated with conducting lending and project-financing transactions, the Bank applies the following types of collateral for recovery of loans and fulfillment of obligations:

- pledge of equipment and goods in turnover;
- pledge of real property (mortgage) and title;
- pledge of rights of demand and construction.

Analysis of the Bank's loan portfolio, net of impairment allowance, by types of collateral is provided in Note 11.

Collateral is not generally held over loans and deposits, except where securities are held as collateral in reverse repurchase agreements. Collateral is not required against exposures to securities.

Quality of the collateral provided is assessed by the following criteria: safety, adequacy and liquidity.

The Bank assumes that the fair value of the collateral is its value estimate recognized by the Bank to calculate the discounted impairment allowance based on its liquidity and possibility of selling such property in the event of borrower's default considering the time needed for such sale, litigation and other costs.

Current market value of the collateral, if necessary, is assessed by accredited appraisers or based on the Bank's internal expert estimate, or carrying amount of the collateral including adjustment coefficient (discount). The Bank's internal expert opinion on the fair value of the collateral and feasibility of the adjustment coefficient (discount), which adjusts the market value, shall be approved/reconciled with the Risk Control Department. The adjustment coefficient (discount) is established based on the table of recommended discounts "Regulations on lending operations" as at initial measurement of the collateral value. Where the market value of the collateral is assessed as impaired, the clients are usually required to provide additional collateral.

Allowance for loan impairment

The Bank creates allowance for loan impairment that represents its estimate of losses incurred in its loan portfolio. The Bank writes off a loan balance against related allowances for loan losses only subject to the approval of the Board of Directors and where the loan is determined as uncollectible and when all necessary steps to collect the loan are completed. Such decision is made after consideration of the information on significant changes in the client's financial position such as inability to repay the loan, and when proceedings from disposal of the collateral are insufficient to cover the debt amount in full. Generally, overdue loans are written off when overdue more than five years or if the debtor is declared bankrupt.

Maximum exposure to credit risk

Maximum credit risk exposure of the Bank as related to financial assets is recorded in their carrying amount.

Credit risk for off balance sheet financial instruments is defined as the possibility of sustaining a loss as a result of another party to a financial instrument failing to perform in accordance with the terms of the contract. The Bank uses the same procedures and methodologies, as defined by the Bank's credit policy, for approving credit related commitments (undrawn loan commitments, letters of credit and guarantees) as it does for on balance sheet credit obligations (loans). Maximum credit risk exposure by credit related commitment represents all the amount of these commitments (Note 18).

(Thousands of Euros)

24. Risk management (continued)

Credit risk (continued)

The Bank monitors credit risk concentrations by industry and geographic location. Analysis of credit risk concentration by industry is presented in Note 11.

The table below shows information on credit risk geographical concentration as of 31 December 2011 and 2010:

	2011								
	Russian Federation	*Czech Republic*	*Republic of Bulgaria*	*Romania*	*Slovak Republic*	*Republic of Cuba*	*Mongolia*	*Other countries*	*Total*
Assets:									
Cash and cash equivalents	611	9,503	3,023	–	–	–	–	764	**13,901**
Deposits with banks and other financial institutions	10,036	6,005	10,044	–	10,032	–	–	75,127	**111,244**
Available-for-sale investment securities	40,869	4,106	4,878	4,093	5,881	–	1,115	7,894	**68,836**
Held-to-maturity investment securities	423	–	–	–	–	–	–	–	**423**
Loans to customers	30,454	–	2,930	–	3,876	–	13,699	–	**50,959**
Other assets	1,427	–	–	–	–	22	–	2	**1,451**
Total	**83,820**	**19,614**	**20,875**	**4,093**	**19,789**	**22**	**14,814**	**83,787**	**246,814**

	2010								
	Russian Federation	*Czech Republic*	*Republic of Bulgaria*	*Romania*	*Slovak Republic*	*Republic of Cuba*	*Mongolia*	*Other countries*	*Total*
Assets:									
Cash and cash equivalents	404	9,008	10,139	–	10,007	–	–	60,165	**89,723**
Deposits with banks and other financial institutions	10,025	–	–	–	10,021	–	–	10,006	**30,052**
Financial instruments at fair value through profit or loss:									
- *Combined financial instruments*	–	–	–	–	–	–	–	15,732	**15,732**
Available-for-sale investment securities	25,552	4,038	5,038	4,198	4,762	–	1,171	14,049	**58,808**
Held-to-maturity investment securities	407	–	–	–	–	–	–	–	**407**
Loans to customers	38,628	–	2,872	–	1,001	–	12,551	–	**55,052**
Other assets	1,654	–	–	–	–	22	459	3	**2,138**
Total	**76,670**	**13,046**	**18,049**	**4,198**	**25,791**	**22**	**14,181**	**99,955**	**251,912**

Other countries include members of the Organization for Economic Development (OECD).

The assessment of credit quality of assets is based on the qualitative and quantitative assessment of credit risk.

Deposit contracts with banks and other financial institutions are concluded with first-class counterparties with high credit ratings assigned by such internationally recognized rating agencies as Standard & Poor’s, Fitch and Moody’s.

(Thousands of Euros)

24. Risk management (continued)

Credit risk (continued)

Assessment of credit quality of loans is based on a 5 grade system of risk factor categories: standard, sub-standard, doubtful, impaired and uncollectible. The risk factor category is assigned on the basis of the assessment of the client's financial position, payment discipline, credit history, compliance with business plan and production discipline, additional characteristics such as management quality, compliance with other terms and conditions of the loan agreement, strength of positions in the market, competitive potential, administrative resources, industry specifics and country rating.

The following table provides information on the credit quality of the loans issued and included in the Bank's loan portfolio as of 31 December 2011:

	Loan amount	*Impairment*	*Loan amount, including impairment*	*Impairment to loan amount ratio, %*
Loans without any signs of impairment identified				
Standard loans				
- Mongolia	7,314	–	7,314	–
- Slovak Republic	3,876	–	3,876	–
Impaired loans				
Loans not past due				
- Russian Federation	23,273	(2,861)	20,412	12
Loans overdue from 90 days to 1 year				
- Russian Federation	17,311	(9,045)	8,266	52
Uncollectible loans				
- Russian Federation	59,075	(57,299)	1,776	97
- Republic of Bulgaria	2,930	–	2,930	–
- Mongolia	11,911	(5,526)	6,385	46
Total loans to customers	**125,690**	**(74,731)**	**50,959**	**59**

The following table provides information on the credit quality of the loans issued and included in the Bank's loan portfolio as of 31 December 2010:

	Loan amount	*Impairment*	*Loan amount, including impairment*	*Impairment to loan amount ratio, %*
Loans without any signs of impairment identified				
Standard loans				
- Mongolia	6,000	–	6,000	–
- Slovak Republic	1,001	–	1,001	–
Impaired loans				
Loans not past due				
- Russian Federation	35,125	(2,413)	32,712	7
Loans overdue from 90 days to 1 year				
- Russian Federation	25,635	(19,719)	5,916	77
- Mongolia	11,048	(4,497)	6,551	41
Uncollectible loans				
- Russian Federation	50,151	(50,151)	–	100
- Republic of Bulgaria	2,880	(8)	2,872	0
- Mongolia	915	(915)	–	100
Total loans to customers	**132,755**	**(77,703)**	**55,052**	**59**

Where possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due. Renegotiated structured loans are continuously reviewed to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual impairment assessment, calculated using the loan's original effective interest rate.

(Thousands of Euros)

24. Risk management (continued)

Liquidity risk

Liquidity risk is the risk of loss resulting from the Bank's inability to meet its payment obligations in full. Liquidity risk results from improper balance between the Bank's financial assets and financial liabilities by period and amount (including due to untimely discharge of its financial obligations by one or several counteragents of the Bank) and/or an unforeseen need of immediate and simultaneous discharge of its financial obligations.

The Bank's approach to management of liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its obligations when due, under both normal and stressed conditions, without incurring unacceptable losses or taking risk of damage to the Bank's reputation.

In the course of liquidity management the Bank's management relies on the following principles:

- liquidity has priority over return;
- continuous liquidity management;
- distribution of authorities between management bodies and divisions;
- planning and limitation of liquidity consistent with the size, nature of business and financial position of the Bank;
- forecasting of cash flows.

Liquidity risk is managed to ensure the Bank's ability to meet its financial obligations in full and on a timely basis. For this purpose the Bank:

- determines an acceptable liquidity level;
- continuously monitors liquidity;
- takes measures to maintain liquidity at the acceptable level;
- in case of liquidity crisis performs a set of procedures for its recovery.

The Bank manages its liquidity in two areas: the Treasury Department manages the liquidity, and Risk Control Department performs control over risk liquidity.

The Treasury Department receives on a weekly basis information from business units regarding the liquidity profile of their financial assets and liabilities and forecasts of projected cash flows arising from projected future business. Further, the Treasury Department manages the Bank's liquidity in accordance with the existing regulatory documents of the Bank and ALRCO's decisions.

The Risk Control Department performs control on a weekly basis over actual values of the current and overall liquidity and compares these values with standards. In case of non-compliance of these standards, the Risk Control Department immediately notifies ALRCO about it in order to develop and perform activities for recovering liquidity.

Due to the fact that all the Bank's liabilities are short-term with maturity "on demand" or "less than 1 month", the Bank does not estimate non-discounted cash flows since the expected cash outflow will not be significantly different from the carrying value of the Bank's financial liabilities as of 31 December 2011 and 31 December 2010.

(Thousands of Euros)

24. Risk management (continued)

Liquidity risk (continued)

The following tables provide an analysis of assets and liabilities on the basis of the remaining period from the balance sheet date to the contractual maturity date (liquidity gap).

	2011							
	Less than 1 month	*1 to 3 months*	*3 months to 1 year*	*1 to 5 years*	*Over 5 years*	*No stated maturity*	*Past due*	*Total*
Assets:								
Cash and cash equivalents	8,899	5,002	–	–	–	–	–	**13,901**
Deposits with banks and other financial institutions	30,111	81,133	–	–	–	–	–	**111,244**
Available-for-sale investment securities	314	812	14,487	35,964	17,259	2,199	–	**71,035**
Held-to-maturity investment securities	20	–	403	–	–	–	–	**423**
Loans to customers less allowance for impairment	–	445	1,968	26,554	2,635	–	19,357	**50,959**
Assets held for sale	–	–	2,048	–	–	–	–	**2,048**
Investment property	–	–	–	–	–	50,287	–	**50,287**
Property and equipment	–	–	–	–	–	49,940	–	**49,940**
Other assets	588	173	690	–	–	–	–	**1,451**
	39,932	**87,565**	**19,596**	**62,518**	**19,894**	**102,426**	**19,357**	**351,288**
Liabilities:								
Due to banks and other financial institutions	1	–	–	–	–	–	–	**1**
Current customer accounts	2,382	–	–	–	–	–	–	**2,382**
Other liabilities	2,067	196	3,510	–	–	–	–	**5,773**
	4,450	**196**	**3,510**	**–**	**–**	**–**	**–**	**8,156**
Net position	**35,482**	**87,369**	**16,086**	**62,518**	**19,894**	**102,426**	**19,357**	**343,132**
Accumulated net position	**35,482**	**122,851**	**138,937**	**201,455**	**221,349**	**323,775**	**343,132**	

	2010							
	Less than 1 month	*1 to 3 months*	*3 months to 1 year*	*1 to 5 years*	*Over 5 years*	*No stated maturity*	*Past due*	*Total*
Assets:								
Cash and cash equivalents	30,685	59,038	–	–	–	–	–	**89,723**
Deposits with banks and other financial institutions	20,045	10,007	–	–	–	–	–	**30,052**
Financial instruments at fair value through profit or loss:								
- *Combined financial instruments*	143	10,496	5,093	–	–	–	–	**15,732**
Available-for-sale investment securities	1,265	456	5,629	23,870	27,588	3,374	–	**62,182**
Held-to-maturity investment securities	–	–	20	387	–	–	–	**407**
Loans to customers less allowance for impairment	1,374	1,532	6,320	30,486	–	–	15,340	**55,052**
Investment property	–	–	–	–	–	47,951	–	**47,951**
Property and equipment	–	–	–	–	–	47,512	–	**47,512**
Other assets	915	180	1,043	–	–	–	–	**2,138**
	54,427	**81,709**	**18,105**	**54,743**	**27,588**	**98,837**	**15,340**	**350,749**
Liabilities:								
Due to banks and other financial institutions	982	–	–	–	–	–	–	**982**
Current customer accounts	2,254	–	–	–	–	–	–	**2,254**
Other liabilities	2,573	255	3,548	–	–	–	–	**6,376**
	5,809	**255**	**3,548**	**–**	**–**	**–**	**–**	**9,612**
Net position	**48,618**	**81,454**	**14,557**	**54,743**	**27,588**	**98,837**	**15,340**	**341,137**
Accumulated net position	**48,618**	**130,072**	**144,629**	**199,372**	**226,960**	**325,797**	**341,137**	

(Thousands of Euros)

24. Risk management (continued)

Liquidity risk (continued)

The table below shows the contractual expiry by maturity of the Bank's financial commitments and contingencies. Each undrawn loan commitment is included in the time band containing the earliest date it can be drawn down.

	Less than 3 months	*3 to 12 months*	*1 to 5 years*	*Over 5 years*	*Total*
2011	14,139	10,000	–	–	**24,139**
2010	11,545	–	–	–	**11,545**

The Bank expects that not all of the contingent liabilities or commitments will be drawn before expiry of the commitments.

Market risk is the risk that the Bank may incur losses due to adverse changes in the market situation expressed in changes in interest rates, exchange rates and value of equity instruments. Market risk is divided into interest rate, currency and equity risks. Market risk is connected to fluctuations on the three main economic markets: debt securities market, equities market, FX and commodities markets, which are subject to general and specific market movements.

The Board of the Bank performs overall management of market risk in line with the General Risk Management Policies approved by the Bank's Council.

ALCO, led by the Deputy Chairman of the Bank's Management Board, coordinates the Bank's market risk management policy, considers and provides to the Management Board recommendations on management of market risks, as well as assets and liabilities.

The objective of market risk management is to manage and control market risk exposures within acceptable parameters, whilst optimizing the return on risk. In stressed market conditions caused by the global economic crisis these activities on market risk management shall be hardened.

Therefore, the regulatory base is enhanced, including setting new stop-out and stop-loss limits and sublimits, subject to positions taken and the limit of overall portfolio losses.

The market risk is mainly managed through daily reassessment of market price positions; optimization of the maturities and raising funds ensuring a stable interest margin; hedging changes in foreign currency position through use of derivative instruments; setting and complying with respective limits which restrict exposure to equity, interest and currency risks.

Currency risk

Foreign currency risk is the risk of loss resulting from adverse changes in exchange rates with respect to the Bank's open positions in foreign currencies.

The currency risk is analyzed through regular estimation of the open currency position with breakdown by currencies and certain balance sheet positions with consideration of maturities/terms of borrowings denominated in foreign currencies.

The currency risk is monitored through regular preparation of analytical materials related to currency and finance markets of the countries of placements and borrowings, which includes required information on quotes, interest rates, exchange rates and trends of their movements.

If necessary, the bank makes adjustments to the asset and liability currency structure to minimize the currency risk. The currency risk is managed through:

- establishing of and compliance with the limits of two levels, including limits of the open currency position and limits for currency operations performed by officials and business units of the Bank (operational limits).

The table below indicates the currencies to which the Bank had significant exposure at 31 December 2011 and 31 December 2010 on its non-trading monetary assets and liabilities and its projected cash flows. The analysis calculates the effect of a reasonably possible movement of the currency rate against the euro on the separate income statement (due to the fair value of currency sensitive non-trading monetary assets and liabilities). The effect on equity does not differ from the effect on the income statement. All other variables are held constant. A negative amount in the table reflects a potential net reduction in the income statement or equity, while a positive amount reflects a net potential increase.

Currency	*Change in currency rate in % 2011*	*Effect on profit 2011*	*Change in currency rate in % 2010*	*Effect on profit 2010*
RUB	+12/-12	1,431/(1,125)	+11/-11	–/(–)
USD	+13/-13	527/(406)	+11/-11	884/(695)

(Thousands of Euros)

24. Risk management (continued)

Currency risk (continued)

The Bank's exposure to currency risk is presented below:

	2011					*2010*				
	EUR	*USD*	*RUB*	*Other currencies*	*Total*	*EUR*	*USD*	*RUB*	*Other currencies*	*Total*
Assets:										
Cash and cash equivalents	13,062	253	575	11	**13,901**	89,183	209	322	9	**89,723**
Deposits with banks and other financial institutions	111,244	–	–	–	**111,244**	30,052	–	–	–	**30,052**
Financial instruments at fair value through profit or loss										
- *Combined financial instruments*	–	–	–	–	**–**	15,732	–	–	–	**15,732**
Available-for-sale investment securities	57,345	3,314	10,376	–	**71,035**	52,885	6,413	2,884	–	**62,182**
Held-to-maturity investment securities	–	423	–	–	**423**	–	407	–	–	**407**
Loans to customers less allowance for impairment	50,959	–	–	–	**50,959**	55,052	–	–	–	**55,052**
Assets held for sale	–	–	2,048	–	**2,048**	–	–	–	–	**–**
Investment property	50,287	–	–	–	**50,287**	47,951	–	–	–	**47,951**
Property and equipment	49,940	–	–	–	**49,940**	47,512	–	–	–	**47,512**
Other assets	245	43	1,163	–	**1451**	213	532	1,393	–	**2,138**
	333,081	**4,033**	**14,162**	**11**	**351,288**	**338,580**	**7,561**	**4,599**	**9**	**350,749**
Liabilities:										
Due to banks and other financial institutions	–	1	–	–	**1**	–	–	982	–	**982**
Current customer accounts	2,182	200	–	–	**2,382**	2,012	242			**2,254**
Other liabilities	1,801	305	3,667	–	**5,773**	1,857	834	3,685	–	**6,376**
	3,983	**506**	**3,667**	**–**	**8,156**	**3,869**	**1,076**	**4,667**	**–**	**9,612**
Net balance sheet position	**329,098**	**3,527**	**10,495**	**11**	**343,132**	**334,711**	**6,485**	**(68)**	**9**	**341,137**

(Thousands of Euros)

24. Risk management (continued)

Interest rate risk

The interest rate risk is the risk of financial losses due to adverse changes in the interest rates of the Bank's assets, liabilities and off-balance sheet instruments.

The Bank is exposed to the effects of fluctuations in the prevailing levels of market interest rates in its financial position and cash flows. Interest margins may increase as a result of such changes but may also reduce or create losses in the event that unexpected movements arise. The Management Board is responsible for overall management of the Bank's assets and liabilities. Due to insignificant amount of borrowings, currently the effect of the interest rate risk is not material.

The Bank performs sensitivity analysis of equity using the interest rate gap method for the purpose of controlling financial losses arising from unfavorable changes in interest rates. The interest rate gap method is used to assess changes in equity by using data on mismatch of claims and obligations sensitive to interest rate changes aggregated at given maturity intervals.

The sensitivity of equity (as a result of change in fair value of available-for-sale equity instruments with fixed rates as at 31 December 2011 and 31 December 2010) due to a reasonably possible change in equity indices is presented below. The effect of revaluation of financial assets was calculated based on the assumption that there are parallel shifts in the yield curve.

Country	*Currency*	*Market index*	*Index change 2011*	*Effect on equity 2011*	*Index change 2010*	*Effect on equity 2010*
Russia	RUB	OFZ	+5.5%/-2.0%	1,189/(432)	+4.0%/-1.0%	158/(40)
EU	EUR	Ger Gov	+0.4%/-0.1%	824/(206)	+1.0%/-0.3%	2,568/(770)
USA	USD	US Treas	+0.6%/-0.2%	11/(4)	+1.3%/-0.3%	208/(48)

Equity risk

Equity risk is the risk of losses due to adverse changes in the market prices for equity instruments (securities) and derivatives that were acquired by the Bank, caused by factors related both to issuers and overall fluctuations in the equity market.

The equity risk is managed through strict compliance with the established limits. To minimize the equity risk, in the course of its activity the Bank may establish the following limits: limit on overall securities portfolio; limit on non-investment grade securities; maximum limit on trading and investment securities portfolio; limit on combined financial instruments portfolio; industry limits; limits by counterparty and issuer; stop-out and stop-loss limits and sublimits on the overall portfolio and individual portfolios. The equity risk is also minimized by hedging changes in the market value of securities through use of derivatives, as well as by using the delivery-versus-payment principle in settlements under securities transactions.

The effect on equity (as a result of change in fair value of equity instruments recognized as available for sale as at 31 December 2011 and 31 December 2010) due to a reasonably possible change in equity indices, with all other variables held constant, is as follows:

Market index	*Index change 2011*	*Effect on equity 2011*	*Index change 2010*	*Effect on equity 2010*
Index S&P 500	+30	456	+18	732
Index S&P 500	-30	(456)	-18	(732)

(Thousands of Euros)

24. Risk management (continued)

Business risks

The Bank's business risks include strategic, legal and reputation risks.

Strategic risk is a risk of losses which the Bank may incur as result of mistakes in making decisions, defining the Bank's business and development strategy, and is expressed in the following:

- Inadequate accounting for potential threats to the Bank's operation;
- Incorrect or insufficiently reasoned definition of perspective business areas;
- Lack of or insufficient resources required (financial, material and technical, human resources) and organizational activities (management decisions).

Legal risk is a risk of losses which the Bank may incur due to:

- The Bank's non-compliance with the legislation and other regulations of the country of residence and country of placement of funds, and agreements entered into;
- Lack of diligence and due care exercised by the Bank's lawyers in the course of preparation of contractual documents failing to provide full protection of the Bank's interests;
- Misconduct of counterparties to the agreements entered into;
- Untimely or unqualified protection of the Bank's interest in court;
- Untimely or unqualified preparation and codification of the Bank's regulations, including those related to risk management.

Risk of the Bank's business reputation loss (reputation risk) is a risk of loss arising from deterioration of the public opinion related to the Bank's financial stability, quality of its services and nature of its business in general resulting in loss of clients (counterparties).

The Bank has developed special procedures and takes measures to minimize adverse effect of business risks for the Bank.

25. Fair values of financial instruments

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by a quoted market price.

The estimated fair values of financial instruments have been determined by the Bank using available market information, where it exists, and appropriate valuation methodologies. However, judgment is necessarily required to interpret market data to determine the estimated fair value. While Management has used available market information in estimating the fair value of financial instruments, the market information may not be fully reflective of the value that could be realized in the current circumstances.

Deposits with banks and other financial institutions and cash and cash equivalents. Management has estimated that at 31 December 2011 and 31 December 2010 the fair value of deposits with banks and other financial institutions and cash and cash equivalents was not materially different from their respective carrying amount. This is due to the fact that it is practice to renegotiate interest rates to reflect current market conditions and, therefore, a majority of balances carry interest at rates approximating market interest rates.

Loans to customers. Management has estimated that at 31 December 2011 and 31 December 2010 the fair values of loans to customers were not materially different from their respective carrying amounts. Fair values of loans to customers were calculated based on the respective market interest rates at 31 December 2011 and 31 December 2010.

(Thousands of Euros)

25. Fair values of financial instruments (continued)

Set out below is a comparison of the carrying amounts and fair values of the Bank's financial instruments that are carried in the financial statements. The table does not include the fair values of non-financial assets and non-financial liabilities.

	Carrying amount 2011	*Fair value 2011*	*Unrecognized gain/(loss) 2011*	*Carrying amount 2010*	*Fair value 2010*	*Unrecognized gain/(loss) 2010*
Financial assets						
Cash and cash equivalents	13,901	13,901	–	89,723	89,723	–
Deposits with banks and other financial institutions	111,244	111,244	–	30,052	30,052	–
Loans to customers	50,959	50,959	–	55,052	55,052	–
Held-to-maturity investment securities	423	363	(60)	407	420	13
Financial liabilities						
Due to banks and other financial institutions	1	1	–	982	982	–
Current customer accounts	2,382	2,382	–	2,254	2,254	–
Total unrecognized change in unrealized fair value			**(60)**			**13**

The following describes the methodologies and assumptions used to determine fair values of those financial instruments which are not already recorded at fair value in the financial statements.

For financial assets and financial liabilities that are liquid or having a short term maturity (less than three months) it is assumed that the carrying amounts approximate their fair value. This assumption is also applied to demand deposits, savings accounts without a specific maturity and variable rate financial instruments.

Fixed rate financial instruments

The fair value of fixed rate financial assets and liabilities carried at amortized cost is estimated by comparing market interest rates when they were first recognized with current market rates offered for similar financial instruments. The estimated fair value of fixed interest bearing loans and deposits with banks is based on discounted cash flows using prevailing money-market interest rates for debts with similar credit risk and maturity.

Financial instruments recorded at fair value

The Bank uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities
- Level 2: techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly
- Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

	Level 1 2011	*Level 2 2011*	*Level 3 2011*	*Total 2011*
Financial assets				
Available-for-sale investment securities	71,035	–	–	**71,035**

	Level 1 2010	*Level 2 2010*	*Level 3 2010*	*Total 2010*
Financial assets				
Combined financial instruments	–	15,732	–	**15,732**
Available-for-sale investment securities	62,182	–	–	**62,182**

(Thousands of Euros)

26. Related party disclosures

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions as defined by IAS 24, *Related Party Disclosures*. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

Transactions and settlements with related parties were carried out on conditions similar to those, which prevail in transactions between independent parties.

The volumes of related party transactions, outstanding balances at the year end, and related expense and income for 2011 and 2010 are as follows:

		2011		***2010***	
	Related party	***Carrying amount***	***Average interest rate, %***	***Carrying amount***	***Average interest rate, %***
Separate statement of financial position					
Loans to customers before allowance for impairment	Subsidiary	8,033	4.0	–	–
Less: allowance for loan impairment	Subsidiary	(1,326)	–	–	–
Loans to customers	Subsidiary	**6,707**	**–**	**–**	**–**
Current customer accounts	Key management personnel	149	1.0	503	0.7

		2011	***2010***
	Related party	***Income/ (expense)***	***Income/ (expense)***
Separate income statement			
Interest income on loans to customers	Subsidiary	48	–
Interest expense on current customer accounts	Key management personnel	(5)	(2)
Net interest income/(expense)		**43**	**(2)**
Reversal of allowance for loan impairment	Subsidiary	2,313	–
Net interest income/(expense) after allowance for loan impairment		**2,356**	**(2)**
Employee benefits	Key management personnel	(670)	(619)
Compensation for travel expenses and medical insurance	Key management personnel	(51)	(49)
Operating expenses		**(721)**	**(668)**
Net profit/(loss) for the year		**1,635**	**(670)**

27. Capital adequacy

Capital adequacy ratio is the most important financial indicator characterizing credibility of the credit institutions and is estimated as ratio of capital base to risk weighted assets expressed as a percentage. Approval of the capital adequacy ratio is the sole power of the Bank's Board of Directors.

The Basel Committee on Banking Regulations recommends maintaining the ratio of capital to risk weighted assets ("statutory capital ratio") above the prescribed minimum level. As at 31 December 2011, this minimum level was 8% (2010 – 8%).

(Thousands of Euros)

27. Capital adequacy (continued)

Taking into account the Bank's status, the structure of the Bank's member countries and respective decision of the Board of Directors, the Bank maintains the capital adequacy ratio at the level not less than 25% as of 31 December 2011 (2010 – 25%).

Therefore, the Bank monitors the capital adequacy ratio, computed in accordance with the Basel Capital Accord (commonly known as Basel I) as defined in the International Convergence of Capital Measurement and Capital Standards (updated April 1998) and Amendment to the Capital Accord to incorporate market risks (updated November 2007).

The following table shows the composition of the Bank's capital position computed in accordance with the Basel Accord, as of 31 December 2011 and 2010.

	2011	*2010*
Tier 1 capital	**314,392**	**312,739**
Paid-in capital	214,495	214,495
Retained earnings	99,897	98,244
Tier 2 capital	**28,740**	**28,398**
Revaluation reserve for available-for-sale investment securities	(2,351)	553
Revaluation reserve for property and equipment	31,091	27,845
Total regulatory capital	**343,132**	**341,137**
Risk-weighted assets:		
Banking book	179,564	176,224
Trading book	51,757	71,953
Total risk-weighted assets	**231,321**	**248,177**
Total capital expressed as a percentage of risk-weighted assets ("capital adequacy ratio")	148.34%	137.46%
Total tier 1 capital expressed as a percentage of risk-weighted assets ("tier 1 capital ratio")	135.91%	126.01%

28. Events after the reporting period

On 17 February 2012 the Bank sold its 100% interest in the share capital of LLC StroyProektInvest to a third party for EUR 0.25 thousand paid in cash.

(The end)