



ANNUAL REPORT
2009

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Chairman's Statement

For the Year Ended 31 December 2009

I am pleased to present the Izola Bank results for the year ended 31 December 2009; despite the current slowdown in economic activity being experienced on a global basis, the 2009 results were in line with 2008 figures which in turn had been very respectable.

Review of performance

During the year ended 31 December 2009, the Bank generated a profit before tax of EUR1,558,972. Profit after tax was EUR1,398,270, an increase of 1.8% over the previous year.

Net interest income decreased by 8.7% when compared to the previous year. The downward re-pricing of the rate of interest receivable on debt securities took place during 2009 which led to a reduction in overall interest receivable. In addition, the interest spread on certain balance sheet items such as shareholders' equity was compressed due to the prevailing very low interest rates.

The contraction in net interest income was largely compensated for by an increase in net fees and commission income which was 13.9% above that earned in the previous year. Income derived from factoring activities largely contributed to the increase in commission income.

Operating expenses decreased by 2.5% in the year under review due to cost control measures as well as cost efficiencies derived from increased automation of operational processes.

Review of financial position

Total assets increased by 18.8% to EUR70,472,655 whereas customer deposits rose from EUR45,196,148 to EUR53,915,259 – an increase of 19.3%. Shareholders' equity amounted to EUR13,594,177 compared with EUR11,746,725 of a year earlier.

As at 31 December 2009 the Capital Adequacy Ratio of 79% and Liquidity Ratio of 220% were both well above the European and US banking sector norms.

There was no sign of deterioration in asset quality in 2009. 71% of the loan book is cash secured by amounts owed to customers held by the Bank. The current credit approval and monitoring structures have helped to ensure very good credit quality of factoring debtors and minimised losses. In fact out of a total amount of EUR79,530,403 of invoices factored over a seven year period, only one amount of EUR82,020 pertaining to a single debtor was written off in 2008.

The Bank's conservative funding and liquidity policies effectively mean that no reliance is made on the short-term inter-bank or commercial paper market for funding the loan book. Nor does the Bank engage in proprietary trading.

Chairman's Statement

For the Year Ended 31 December 2009

Looking ahead

The Bank is committed to further develop the factoring and credit card business in 2010 and beyond. In addition measures will be taken to further promote short term credit facilities in the Bank's target market. A new marketing campaign will be launched in 2010 advertising increased credit card limits as well as introducing a new overdraft facility.

In order to fund these initiatives and ultimately support the future growth and expansion of the Bank, the Board of Directors have proposed a bond issue which will be listed on the Malta Stock Exchange subject to regulatory approval.

In 2010 the Bank will finalise the acquisition and refurbishment of new premises which will house the Bank's new disaster recovery site. The Bank's main computer hardware will also be upgraded in order to provide for real time transfer of data to the recovery site. These actions will ensure a more positive customer experience by guaranteeing continuity of service delivery. It is expected that the new disaster recovery site will be fully operational by June 2010.

Conclusion

On behalf of the Board I would like to thank our customers for their loyalty and support. Finally I would like to express my thanks to the management team and staff members for their continuing hard work and commitment to the Bank.



Mr. Carl Van Marcke
Chairman - Izola Bank Limited

Directors' Report

For the Year Ended 31 December 2009

The directors present their report together with the financial statements of Izola Bank Limited ("the bank") for the year ended 31 December 2009.

Board of directors:

Mr. Carl Van Marcke (Chairman)
Mrs. Magdalena De Roeck (Deputy Chairperson)
Countess A. d'Oultremont
Mr. Peter Van Marcke
Mr. Frederick E. Amato-Gauci
Mr. John Melillo
Mr. Joseph Caruana
Mr. Charles Hertogs (appointed on 4 January 2010)
Mr. Patrick Van Leynseele (appointed on 4 January 2010)

Company secretary

Mr. Stefan Farrugia

Results for the year

The bank reported a profit after tax of EUR1,398,270 for the year under review. Further information on the results is provided in the Chairman's Statement which immediately precedes this Director's Report.

Principal activities

Izola Bank Limited is registered in Malta as a limited liability company under the Companies Act, 1995 (Chapter 386, Laws of Malta). The bank is licensed by the Malta Financial Services Authority to carry out the business of banking in terms of the Banking Act, 1994 (Chapter 371, Laws of Malta). The bank is principally engaged in providing corporate banking services to non-resident customers.

Review of financial performance and future developments

A review of the bank's financial performance for the year ended 31 December 2009 and a summary of likely future developments are given in the Chairman's Statement which immediately precedes this Directors' Report.

Events occurring after balance sheet date

On 15 February 2010, the shareholders of the bank resolved to change the status of Izola Bank from a private limited liability company to that of a public limited liability company.

Subject to applicable regulatory approval, on the same date, the Board of Directors approved a base Prospectus for a debt issuance programme for an aggregate of EUR28,000,000 secured bonds and the issuance thereunder of a first tranche of EUR7,000,000 Secured Bonds 2015 subject to an over-allotment option of EUR2,000,000.

Dividends

A net interim dividend of EUR7,000,000 was declared and paid on 9 October 2009 representing a net dividend per share of EUR43.75. No final dividend is being recommended.

Reserves

On 29 December 2009, the bank's shareholders by virtue of formal Capital Contribution Agreements, contributed an amount of EUR7,449,182 to the distributable reserves of the bank.

Moreover, the bank has transferred an amount of EUR51,417 from retained earnings to the Depositor Compensation Scheme Reserve.

Directors

The Directors at the date of this report are listed above. Mr. Charles Hertogs and Mr Patrick Van Leynseele were appointed on 4 January 2010, while Mr Louis de Spirlet retired from the Board on 11 December 2009.

Directors' responsibilities

The Companies Act, 1995 (Chapter 386, Laws of Malta) requires the Directors of Izola Bank Limited to prepare financial statements for each financial period which give a true and fair view of the financial position of the bank as at the end of the financial year and of the profit or loss of the bank for that period in accordance with the requirements of International Financial Reporting Standards as adopted by the EU.

Directors' responsibilities (continued)

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy, at any time, the financial position of the bank and to enable them to ensure that the financial statements have been properly prepared in accordance with the provisions of the Companies Act, 1995 (Chapter 386, Laws of Malta) and the Banking Act, 1994 (Chapter 371, Laws of Malta).

The Directors are also responsible for safeguarding the assets of the bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors, through oversight of management, are responsible to ensure that the bank establishes and maintains internal control to provide reasonable assurance with regard to reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations.

Management is responsible, with oversight from the Directors, to establish a control environment and maintain policies and procedures to assist in achieving the objective of ensuring, as far as possible, the orderly and efficient conduct of the bank's business. This responsibility includes establishing and maintaining controls pertaining to the bank's objective of preparing financial statements as required by the Act and managing risks that may give rise to material misstatements in those financial statements. In determining which controls to implement to prevent and detect fraud, management considers the risks that the financial statements may be materially misstated as a result of fraud.

Auditors

KPMG have expressed their willingness to continue in office. A resolution proposing the re-appointment of KPMG as auditors of the bank will be submitted at the forthcoming Annual General Meeting.

Approved by the Board of Directors on 15 February 2010 and signed on its behalf by:



Mr. Peter Van Marcke
Director



Countess A. d'Oultremont
Director

Registered Address

53-58, East Street, Valletta VLT 1251, Malta.

Statement of Financial Position

For the Year Ended 31 December 2009

	Note	2009 EUR	2008 EUR
ASSETS			
Cash		850	779
Balances with Central Bank of Malta		504,998	385,852
Investments	13	28,945,952	26,307,884
Loans and advances to banks	14	11,219,096	9,788,398
Factored receivables	15	5,338,919	4,362,518
Other loans and advances to customers	16	21,140,261	15,030,861
Property and equipment	17	2,016,686	2,009,850
Other assets	18	1,305,893	1,423,935
Total assets		70,472,655	59,310,077
LIABILITIES			
Balance with Central Bank of Malta		1,500,000	-
Amounts owed to customers	19	53,915,259	45,196,148
Deferred tax liabilities	20	347,228	382,449
Current tax payable		230,043	228,666
Accruals and deferred income	21	885,948	1,756,089
Total liabilities		56,878,478	47,563,352
EQUITY			
Called up share capital	22	4,000,000	4,000,000
Property revaluation reserve	22	640,483	647,695
Depositor compensation scheme reserve	22	51,417	-
Capital contribution	22	7,449,182	-
Retained earnings	22	1,453,095	7,099,030
Total equity attributable to equity holders of the bank		13,594,177	11,746,725
Total liabilities and equity		70,472,655	59,310,077
Memorandum items			
Commitments	23	6,835,420	5,917,759

The notes on pages 12 to 45 are an integral part of these financial statements.

The financial statements on pages 8 to 45 were approved by the Board of Directors on 15 February 2010 and signed on its behalf by:



Mr. Peter Van Marcke
Director



Countess A. d'Oultremont
Director

Statement of Changes in Equity

For the Year Ended 31 December 2009

	Share Capital EUR	Revaluation Reserve EUR	Depositor Compensation		Retained Earnings EUR	Total EUR
			Scheme Reserve EUR	Capital Contribution EUR		
Balance at 1 January 2008	4,000,000	654,907	-	-	5,718,808	10,373,715
Total comprehensive income for the year						
Profit for the year	-	-	-	-	1,373,010	1,373,010
Other comprehensive income, net of tax						
Transfer of depreciation on revaluation surplus net of deferred tax	-	(7,212)	-	-	7,212	-
Total other comprehensive income, net of tax	-	(7,212)	-	-	7,212	-
Total comprehensive income for the year	-	(7,212)	-	-	1,380,222	1,373,010
Balance at 31 December 2008	4,000,000	647,695	-	-	7,099,030	11,746,725

	Share Capital EUR	Revaluation Reserve EUR	Depositor Compensation		Retained Earnings EUR	Total EUR
			Scheme Reserve EUR	Capital Contribution EUR		
Balance at 1 January 2009	4,000,000	647,695	-	-	7,099,030	11,746,725
Total comprehensive income for the year						
Profit for the year	-	-	-	-	1,398,270	1,398,270
Other comprehensive income, net of tax						
Transfer of depreciation on revaluation surplus net of deferred tax	-	(7,212)	-	-	7,212	-
Transfer from retained earnings	-	-	51,417	-	(51,417)	-
Total other comprehensive income, net of tax	-	(7,212)	51,417	-	(44,205)	-
Total comprehensive income for the year	-	(7,212)	51,417	-	1,354,065	1,398,270
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Dividends paid to equity holders	-	-	-	-	(7,000,000)	(7,000,000)
Contributions paid by equity holders	-	-	-	7,449,182	-	7,449,182
Total contributions by and distributions to owners	-	-	-	7,449,182	(7,000,000)	449,182
Balance at 31 December 2009	4,000,000	640,483	51,417	7,449,182	1,453,095	13,594,177

The notes on pages 12 to 45 are an integral part of these financial statements.

Statement of Comprehensive Income

For the Year Ended 31 December 2009

	Note	2009 EUR	2008 EUR
Interest receivable and similar income			
- on loans and advances	5	1,048,604	1,758,814
- on debt securities		1,674,301	1,770,484
Interest expense	6	(1,261,842)	(1,928,582)
Net interest income		1,461,063	1,600,716
Fees and commission income		990,827	865,027
Fees and commission expense		(32,486)	(23,921)
Net fees and commission income	7	958,341	841,106
Net trading gains	8	11,933	13,208
Other operating income		4,193	4,193
Operating income		2,435,530	2,459,223
Administrative expenses		(614,882)	(630,442)
Depreciation		(253,892)	(238,094)
Impairment allowances	9	(7,784)	(17,011)
Profit before income tax	10	1,558,972	1,573,676
Income tax expense	11	(160,702)	(200,666)
Profit for the year		1,398,270	1,373,010
Other comprehensive income, net of income tax			
Transfer of depreciation on revaluation surplus net of deferred tax			
- retained earnings		7,212	7,212
- revaluation reserve		(7,212)	(7,212)
Other comprehensive income for the year, net of income tax		-	-
Total comprehensive income for the year, net of income tax		1,398,270	1,373,010
Earnings per share	12	8.74	8.58

The notes on pages 12 to 45 are an integral part of these financial statements.

Statement of Cash Flows

For the Year Ended 31 December 2009

	Note	2009 EUR	2008 EUR
Cash flows from operating activities			
Interest and commission receipts		2,127,680	2,629,871
Interest and commission payments		(2,170,820)	(1,322,380)
Payments to employees and suppliers		(688,860)	(528,660)
Operating (loss)/profit before changes in operating assets/liabilities		(732,000)	778,831
Increase in operating assets:			
- loans and advances to customers		(6,109,400)	(775,861)
- factored receivables		(977,554)	(1,447,298)
Increase in operating liabilities:			
- amounts owed to customers		8,719,111	685,276
- amounts owed to banks		1,500,000	-
Net cash generated from/(used in) operations before income tax	24	2,400,157	(759,052)
Income tax paid		(194,547)	(164,209)
Net cash from/(used in) operating activities		2,205,610	(923,261)
Cash flows from investing activities			
Payments to acquire property and equipment		(182,889)	(141,712)
Payments to acquire investments		(1,850,356)	-
Interest received from investments		1,038,253	953,450
Net cash (used in)/from investing activities		(994,992)	811,738
Cash flow from financing activities			
Net capital contribution received		339,297	-
Net cash from financing activities		339,297	-
Net increase/(decrease) in cash and cash equivalents		1,549,915	(111,523)
Cash and cash equivalents at beginning of year		10,175,029	10,286,552
Cash and cash equivalents at end of year	25	11,724,944	10,175,029

The notes on pages 12 to 45 are an integral part of these financial statements.

Notes to the Financial Statements

For the Year Ended 31 December 2009

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Notes to the Financial Statements

For the Year Ended 31 December 2009

1 Reporting Entity

Izola Bank Limited (the “bank”) is a limited liability company domiciled and incorporated in Malta.

2 Basis of Preparation

2.1 Statement of compliance

These financial statements have been drawn up in accordance with International Financial Reporting Standards as adopted by the EU (the “applicable framework”). All references in these financial statements to IAS, IFRS or SIC/IFRIC interpretation refer to those adopted by the EU.

These financial statements have also been prepared and presented in accordance with the provisions of the Companies Act, 1995 (Chapter 386, Laws of Malta), to the extent that such provisions do not conflict with the applicable framework.

2.2 Basis of measurement

The financial statements have been prepared on the historical cost basis except that available-for-sale financial assets are stated at fair value.

The methods used to measure fair values are discussed in note 4.

2.3 Functional and presentation currency

These financial statements are presented in Euro, which is the bank’s functional currency.

2.4 Use of estimates and judgements

The preparation of financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

In particular, information about significant areas of estimation, uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements are described in note 28.

2.5 Changes in accounting policy

Starting as of 1 January 2009, the bank has changed its accounting policy relating to presentation of financial statements.

Presentation of financial statements

The bank applied revised IAS 1, *Presentation of Financial Statements (2007)*, which became effective as of 1 January 2009. As a result, the bank presents in the statement of changes in equity all owner changes in equity, whereas all non-owner changes in equity are presented in the statement of comprehensive income.

Comparative information has been re-presented so that it also is in conformity with the revised standard. The change in accounting policy only impacts presentation aspects.

Notes to the Financial Statements

For the Year Ended 31 December 2009

3 Significant Accounting Policies

The accounting policies set out below have been applied consistently to all periods presented in these financial statements, except as explained in note 2.5 which address changes in accounting policies.

3.1 Financial instruments

3.1.1 *Non-derivative financial instruments*

Non-derivative financial instruments comprise investments in equity and debt securities, cash equivalents and loans and receivables.

Non-derivative financial instruments are recognised initially at fair value plus, for instruments not at fair value through profit or loss, any directly attributable transaction costs. Subsequent to initial recognition, non-derivative financial instruments are measured as described below.

Cash equivalents comprise deposits with contractual maturity of less than three months. Subsequent to initial recognition, cash equivalents are measured at amortised cost.

3.1.1.1 *Held-to-maturity investments*

If the bank has the positive intention and ability to hold debt securities to maturity, then they are classified as held-to-maturity. Held-to-maturity investments are measured at amortised cost using the effective interest method, less any impairment losses.

3.1.1.2 *Available-for-sale financial assets*

The bank's investments in equity securities are classified as available-for-sale financial assets. Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses, and foreign exchange gains and losses on available-for-sale monetary items, are recognised directly in equity. When an investment is derecognised, the cumulative gain or loss in equity is transferred to profit or loss.

3.1.1.3 *Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. These include loans and advances to banks and customers that are recognised on the day the cash is advanced to the borrowers. These are initially recognised at fair value plus transaction costs that are directly attributable to the acquisition of the financial assets. Subsequent to initial recognition, loans and receivables are measured at amortised cost using the effective interest method, less impairment losses.

3.1.2 *Derecognition*

A financial asset is derecognised when the contractual rights to receive the cash flows from the financial asset expire, have been realised or are transferred and control is not retained by the bank, or substantially all the risks and rewards of ownership have been transferred by the bank.

A financial liability is derecognised when it is extinguished, that is when the obligation is discharged, cancelled or expires.

Assets designated by the bank as available-for-sale assets that are sold are derecognised and corresponding receivables from the buyer for the payment are recognised as at the date the bank commits to sell the assets.

Held-to-maturity instruments and loans and receivables are derecognised on the day these are transferred by the bank.

Notes to the Financial Statements

For the Year Ended 31 December 2009

3 Significant Accounting Policies (continued)

3.2 Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

3.3 Property and equipment

3.3.1 Recognition and measurement

Items of property and equipment are measured at cost or revaluation less accumulated depreciation and accumulated impairment losses.

Freehold property is revalued to fair value on the basis of its existing use every five years or earlier, whenever its fair value differs materially from its carrying amount. Revaluations are performed by a professionally qualified architect. Any surpluses arising on such revaluation are credited to a revaluation reserve. Any deficiencies resulting from decreases in value are deducted from this reserve to the extent that it is sufficient to absorb them, with any excess charged to profit or loss thereafter.

Where parts of an item of property and equipment have different useful lives, they are accounted for as separate items of property and equipment.

3.3.2 Subsequent costs

The cost of replacing part of an item of property and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied with the part will flow to the bank and its cost can be measured reliably. The costs of the day-to-day servicing of property and equipment are recognised in profit or loss as incurred.

3.3.3 Depreciation

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property and equipment.

The estimated useful lives for the current and comparative periods are as follows:

Premises and improvements	20 – 100 years
Computer hardware and software	3 – 5 years
Other assets	5 years

Depreciation methods, useful lives and residual values are reviewed at each reporting date.

Notes to the Financial Statements

For the Year Ended 31 December 2009

3 Significant Accounting Policies (continued)

3.4 Impairment

The carrying amounts of the bank's assets, other than deferred tax assets, are reviewed at each balance sheet date to determine whether there is objective evidence of impairment.

A financial asset or group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset and that loss has an impact on the estimated future cash flows of the financial assets or group of financial assets that can be reliably measured. If there is objective evidence, the asset's recoverable amount is estimated.

In the case of other assets, an impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in profit or loss unless the asset is carried at revalued amount, in which case the impairment is treated as a revaluation decrease, to the extent of the credit balance on the revaluation reserve.

3.4.1 *Assets carried at amortised cost*

The recoverable amount of the bank's investments in held-to-maturity securities and receivables carried at amortised cost is calculated as the present value of estimated future cash flows (excluding future credit losses that have not been incurred), discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition of these financial assets). Receivables with a short duration are not discounted.

Loans and advances are presented net of specific and collective impairment allowances for uncollectibility. The bank assesses at each balance sheet date whether there is any objective evidence that a loan is impaired. Specific impairment allowances are determined by an evaluation of the exposures on a case-by-case basis and are made against the carrying amount of loans and advances that are identified as being impaired based on regular reviews of outstanding balances to reduce these loans and advances to their recoverable amounts.

Collective impairment allowances are maintained to reduce the carrying amount of portfolios of financial assets with similar risk characteristics to their estimated recoverable amounts at the balance sheet date. The expected cash flows for portfolios of financial assets with similar risk characteristics are estimated based on, amongst others, observable data and considering the credit rating of the underlying customers and late payments of interest or penalties.

Increases and decreases in the specific and collective impairment allowances are recognised in profit or loss. When a loan is known to be uncollectible, all the necessary legal procedures have been completed, and the final loss has been determined, the loan is written off.

3.4.2 *Financial assets measured at fair value*

The recoverable amount of an equity instrument is its fair value.

When a decline in the fair value of an available-for-sale financial asset has been recognised directly in equity and there is objective evidence that the asset is impaired, the cumulative loss that had been recognised directly in equity is recognised in the statement of comprehensive income even though the financial asset has not been derecognised. The amount of the cumulative loss that is recognised in profit or loss is the difference between the acquisition cost and current fair value, less any impairment loss on that financial asset previously recognised in profit or loss.

3.4.3 *Other assets*

The recoverable amount of other assets is the greater of their net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

Notes to the Financial Statements

For the Year Ended 31 December 2009

3 Significant Accounting Policies (continued)

3.4 Impairment (continued)

3.4.4 Reversals of impairment

An impairment loss in respect of a held-to-maturity asset or receivable carried at amortised cost is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

In respect of other assets, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount and is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar risk characteristics.

All impairment losses are recognised in profit or loss. Any cumulative loss in respect of an available-for-sale financial asset recognised previously in equity is transferred to profit or loss.

An impairment loss can be reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognised. For financial assets measured at amortised cost, the reversal is recognised in profit or loss. For available-for-sale financial assets that are equity securities, the reversal is recognised directly in equity.

3.5 Amounts owed to customers

Amounts owed to customers are initially measured at fair value plus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method, except where the bank chooses to carry the liabilities at fair value through profit or loss.

3.6 Provisions

A provision is recognised if, as a result of a past event, the bank has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

3.7 Interest

Interest income and expense are recognised in profit or loss using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability. The effective interest rate is established on initial recognition of the financial asset and liability and is not revised subsequently.

The calculation of the effective interest rate includes all transaction costs, and discounts or premiums that are an integral part of the effective interest rate. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or liability.

Interest income and expense presented in the statement of comprehensive income include interest on financial assets and liabilities at amortised cost on an effective interest rate basis.

Notes to the Financial Statements

For the Year Ended 31 December 2009

3 Significant Accounting Policies (continued)

3.8 Fees and commission

Fees and commission income and expenses that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate.

Other fees and commission income, including account servicing fees, investment management fees, sales commission, placement fees and syndication fees, are recognised as the related services are performed. When a loan commitment is not expected to result in the draw-down of a loan, loan commitment fees are recognised on a straight-line basis over the commitment period.

Other fees and commissions expense relate mainly to transaction service fees, which are expensed as the services are received.

3.9 Trading gains/losses

Trading gains/losses comprises all realised and unrealised foreign exchange differences.

3.10 Operating lease payments

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease.

3.11 Employee benefits

The bank contributes towards the State pension defined contribution plan in accordance with local legislation and to which it has no commitment beyond the payment of fixed contributions. Obligations for contributions to the defined contribution plan are recognised as an expense in profit or loss as they fall due.

3.12 Foreign currency transactions

Transactions in foreign currencies are recorded in the functional currency at the foreign exchange rate prevailing on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated into the functional currency at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in profit or loss. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated into the functional currency at foreign exchange rates ruling at the dates the fair values were determined. Foreign currency differences arising in retranslation are recognised in profit or loss, except for differences arising on the retranslation of available-for-sale equity instruments.

Notes to the Financial Statements

For the Year Ended 31 December 2009

3 Significant Accounting Policies (continued)

3.13 Income tax

Income tax expense comprises current and deferred tax. Income tax is recognised in profit or loss except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised. Deferred tax assets are reviewed at each balance sheet date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

3.14 Earnings per share

The bank presents basic earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the bank by the weighted average number of ordinary shares outstanding during the period.

3.15 Operating segments

An operating segment is a component of the bank that engages in business activities from which it may earn revenues and incur expenses, including revenue and expenses that relate to transactions with any of the bank's other components, whose operating results are reviewed regularly by the bank's Board of Directors (being the chief operating decision maker), to make decisions about resources allocated to each segment and assess its performance, and for which discrete financial information is available.

3.16 New standards and interpretations not yet adopted

The following new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2009, and have not been applied in preparing these financial statements:

- Amendment to IAS 32 *Financial Instruments: Presentation*: Classification of rights issues
- IFRIC 18 *Transfers of assets from customers*
- Amendments to IFRIC 9 and IAS 39 *Financial Instruments: Recognition and Measurement*: Reassessment of Embedded derivatives
- IFRIC 17 *Distributions of Non-cash assets to owners*
- Amendment to IAS 39 *Financial Instruments: Recognition and Measurement*: Eligible hedged items
- Revised IFRS 3 *Business combinations*
- Amendments to IAS 27 *Consolidated and Separate Financial Statements*.

The bank is currently in the process of evaluating the potential effect of these standards, amendments to standards and interpretations. Given the nature of the bank's operations, these are not expected to have a pervasive impact on the bank's financial statements.

Notes to the Financial Statements

For the Year Ended 31 December 2009

4 Financial Risk Management

4.1 Organisation

The Board of Directors has overall responsibility for the establishment and oversight of the bank's risk management framework. The Board has established the Board Committee, the Audit Committee and the Credit Committee, which are responsible for the monitoring of risk in their specified areas. Executive and non-executive directors sit on these Committees and the Committees report regularly to the Board of Directors on their activities.

Risk management policies have been established to identify and analyse the risks faced by the bank, to set out appropriate risk limits and controls, and to monitor risks and adherence to limits.

The risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The bank has developed appropriate risk management training for the needs of the relevant staff members.

4.2 Risk exposure

The bank is exposed to a number of risks, which it manages at different organisational levels.

The main categories of risk are:

- *Credit risk*: Risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. It arises from the lending, treasury and other activities undertaken by the bank.
- *Market risk*: Risk of losses arising from unfavourable changes in the level and volatility of interest rates, foreign exchange rates or investment prices.
- *Liquidity risk*: Liquidity risk is divided into two-categories:
 - *Market (product) liquidity risk*: risk of losses arising from difficulty in accessing a product or market at the required time, price and volume.
 - *Funding liquidity risk*: risk of losses arising from a timing mismatch between investing, placements and fund raising activities resulting in obligations missing the settlement date or satisfied at higher than normal rates.
- *Operational risk*: Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the bank's processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of the bank's operations and are faced by all business entities.

Notes to the Financial Statements

For the Year Ended 31 December 2009

4 Financial Risk Management (continued)

4.3 Capital base

The bank is a licenced financial services provider and must therefore comply with the capital requirements under the relevant capital requirements laws and regulations. The bank has adopted the Standardised Approach to calculate its capital requirements.

4.3.1 Capital management

The bank must have sufficient capital to comply with regulatory capital requirements. The purpose of the bank's capital management is to ensure an efficient use of capital in relation to risk appetite as well as business development.

The bank's regulatory capital is analysed into two tiers:

- Tier 1 capital, which includes ordinary share capital, capital contribution and retained earnings.
- Tier 2 capital, which includes property revaluation reserve and collective impairment allowances.

Banking operations are categorised as banking book, and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures.

The bank has complied with all capital requirements directives and rules throughout the year.

There have been no material changes in the bank's management of capital during the year.

4.3.2 Calculation of minimum capital requirement and risk-weighted assets

The minimum capital requirements are calculated for the credit, market and operational risk. The capital ratio is calculated using the definition of regulatory capital and risk-weighted assets. The total capital ratio must be no lower than 8%.

Total risk-weighted assets are determined by multiplying the capital requirements for market risk and operational risk by 12.5 (i.e. the reciprocal of the minimum capital ratio of 8%) and adding the resulting figures to the sum of risk-weighted assets for credit risk.

Below is the bank's capital requirements and capital adequacy ratio computation.

	2009	2008
	EUR	EUR
Tier 1 capital		
Ordinary share capital	4,000,000	4,000,000
Capital Contribution	7,449,182	-
Retained earnings	1,453,095	7,099,030
	<u>12,902,277</u>	<u>11,099,030</u>
Tier 2 capital		
Property revaluation reserve	640,483	647,695
Collective impairment allowance	54,646	46,862
	<u>695,129</u>	<u>694,557</u>
Total regulatory capital	<u>13,597,406</u>	<u>11,793,587</u>

Notes to the Financial Statements

For the Year Ended 31 December 2009

4 Financial Risk Management (continued)

4.3 Capital base (continued)

4.3.2 Calculation of minimum capital requirement and risk-weighted assets (continued)

	Balance sheet value	Risk weighted exposure	Capital requirement	Balance sheet value	Risk weighted exposure	Capital requirement
	2009	2009	2009	2008	2008	2008
	EUR	EUR	EUR	EUR	EUR	EUR
On balance sheet assets						
Cash	850	-	-	779	-	-
Balances with						
Central Bank of Malta	504,998	-	-	385,852	-	-
Investments	28,945,952	3,653	292	26,307,884	3,653	292
Loans and advances to banks	11,219,096	2,243,819	179,506	9,788,398	1,957,680	156,614
Factored receivables	5,338,919	5,393,565	431,486	4,362,518	4,409,380	352,751
Other loans and advances to customers	21,140,261	2,423,261	193,861	15,030,861	45,861	3,669
Property and equipment	2,016,686	2,016,687	161,335	2,009,850	2,009,850	160,788
Prepayments and accrued income	1,305,893	652,946	52,236	1,423,935	711,968	56,957
	<u>70,472,655</u>	<u>12,733,931</u>	<u>1,018,716</u>	<u>59,310,077</u>	<u>9,138,392</u>	<u>731,071</u>
Off-balance sheet items						
Commitments	6,835,420	-	-	5,917,759	-	-
		Risk weighted exposure	Capital requirement		Risk weighted exposure	Capital requirement
		EUR	EUR		EUR	EUR
Credit risk capital requirement		12,733,931	1,018,716		9,138,392	731,071
Foreign exchange risk capital requirement		23,250	1,860		13,725	1,098
Operational risk capital requirement		4,423,425	353,874		3,998,625	319,890
Total capital requirement		<u>17,180,606</u>			<u>13,150,742</u>	
Own funds						
Original own funds	12,902,277			11,099,030		
Additional own funds	695,129			694,557		
Total own funds	<u>13,597,406</u>			<u>11,793,587</u>		
Capital adequacy ratio at 31 December			<u>79%</u>			<u>89%</u>

4.4 Credit risk

Credit risk is the risk of financial loss to the bank if a customer or counterparty to the financial instrument fails to meet its contractual obligations, and arises principally from the bank's loans and advances to customers and other investment securities. For risk management reporting purposes, the bank considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk).

The bank follows standards, policies and procedures established by the bank's Board of Directors for the control and monitoring of all risks. The Board of Directors has delegated the responsibility for the management of credit risk to the Board Committee and Credit Committee. The bank's management is responsible for the oversight of the bank's credit risk. The bank's credit risk policies and procedures are reviewed regularly through internal audit.

It is the bank's policy to obtain prime collateral to cover its exposure in case of default. At balance sheet date 91% of other loans and advances to customers and investments were cash secured.

Notes to the Financial Statements

For the Year Ended 31 December 2009

4 Financial Risk Management (continued)

4.4 Credit risk (continued)

4.4.1 Maximum exposure to credit risk

The bank's maximum credit risk exposure to on and off-balance sheet financial instruments, before taking account of any collateral held or other credit enhancements can be classified in the following categories:

- Financial assets recognised on balance sheet comprising balances with Central Bank of Malta, financial investments, factored receivables, loans and advances and acceptances and endorsements. The maximum exposure of these financial assets to credit risk, equals their carrying amount.
- Commitments for factored receivables - the maximum exposure to credit risk is the full amount of the committed facilities (note 23).

4.4.2 Industry concentration

The following industry concentrations relating to loans and advances to customers are considered significant:

	2009		2008	
	EUR	%	EUR	%
Manufacturing	12,303,000	58	10,410,000	69
Wholesale and retail trade	2,541,000	12	3,970,000	26
Real estate, renting and business activities	6,296,261	30	650,861	5
	<u>21,140,261</u>	<u>100</u>	<u>15,030,861</u>	<u>100</u>

4.4.3 Analysis of collateral

The bank holds collateral against loans and advances to customers and investment securities in the form of pledges over deposits held with the bank. Except for pledges over deposits held with the bank, estimates of fair value are based on the value of collateral assessed at the time of borrowing, and generally are not updated except when a loan is individually assessed as impaired. Factored receivables are unsecured and collateral generally is not held over loans and advances to banks.

The fair value of collateral held as security is as follows:

Type of collateral	Carrying amounts of neither past due nor impaired			
	Loans and advances to customers		Investment in debt securities	
	2009 EUR	2008 EUR	2009 EUR	2008 EUR
Deposits held with the bank	<u>18,717,000</u>	<u>14,985,000</u>	<u>27,101,944</u>	<u>26,307,884</u>

Notes to the Financial Statements

For the Year Ended 31 December 2009

4 Financial Risk Management (continued)

4.4 Credit risk (continued)

4.4.4 Impaired factored receivables

These comprise factored receivables for which the bank determines that it is probable that it will be unable to collect all principal and interest due according to the contractual terms of the factored receivables agreements.

	2009 EUR	2008 EUR
Factored receivables - gross	5,393,564	4,409,380
Collectively determined	5,393,564	4,409,380
Allowance for impairment	54,646	46,862

4.4.5 Neither past due nor impaired loans and securities

	2009 EUR	2008 EUR
Loans and advances to customers	21,140,261	15,030,861
Loans and advances to banks	11,219,096	9,788,398
Investment securities	28,945,952	26,307,884
	61,305,309	51,127,143

4.4.6 Past due but not impaired

Receivables where contractual interest or principal payments are past due but the bank believes that impairment is not appropriate on the basis of the level of security / collateral available and / or the stage of collection of amounts owed to the bank.

At 31 December 2009, 15% of the bank's factored receivables were past due but not impaired.

4.4.7 Loans with renegotiated terms

Loans with renegotiated terms are loans that have been restructured due to deterioration in the borrower's financial position and where the bank has made concessions that it would not otherwise consider. Once the loan is restructured it remains in this category independent of satisfactory performance after restructuring.

The bank does not have loans with renegotiated terms.

4.4.8 Allowances for impairment

The bank establishes an allowance for impairment losses that represents its estimate of incurred losses in its factored receivables portfolio. The main components of this allowance are a specific loss component that relates to individually impaired receivables, and a collective loss allowance established for groups of factored receivables in respect of losses that have been incurred but have not been identified and subjected to individual assessment for impairment.

	2009 EUR	2008 EUR
Factored receivables		
Collective allowance for impairment	54,646	46,862

No allowance for impairment was required for specific exposures.

Notes to the Financial Statements

For the Year Ended 31 December 2009

4 Financial Risk Management (continued)

4.4 Credit risk (continued)

4.4.9 Write-off policy

The bank writes off a loan, security and/or factored receivable balance (and any related allowance for impairment losses) when management determines that the loan, security and/or factored receivable is uncollectible. This determination is reached after considering information such as occurrence of significant changes in the borrower / issuer's financial position such that the borrower / issuer can no longer pay the obligation, or that proceeds from collateral will not be sufficient to pay back the entire exposure.

4.4.10 Concentration risk

The bank monitors concentration of credit risk by sector and by geographic location. An analysis of concentrations of credit risk is shown below.

	Loans and advances to customers		Factored receivables		Loans and advances to banks		Investment securities	
	2009 EUR	2008 EUR	2009 EUR	2008 EUR	2009 EUR	2008 EUR	2009 EUR	2008 EUR
Carrying amount	21,140,261	15,030,861	5,338,919	4,362,518	11,219,096	9,788,398	28,945,952	26,307,884
Concentration by sector								
Corporate	21,140,261	15,030,861	5,338,919	4,362,518	-	-	28,942,299	26,304,231
Banks	-	-	-	-	11,219,096	9,788,398	-	-
Equity	-	-	-	-	-	-	3,653	3,653
	21,140,261	15,030,861	5,338,919	4,362,518	11,219,096	9,788,398	28,945,952	26,307,884
Concentration by location								
Europe	21,140,261	15,030,861	5,338,919	4,362,518	11,219,096	9,788,398	28,945,952	26,307,884

Concentration by location for loans and advances to customers and banks and investment securities is measured based on the location of the borrower or issuer of the security.

4.5 Market risk

Market risk comprises the risk of losses in value caused by unexpected changes in market prices (interest rates, equity prices, foreign exchange rates and credit spreads) before the affected positions can be closed out or hedged.

Market risk for the bank consists of three elements:

- Interest rate risk, which is the risk of losses because of changes in interest rates.
- Exchange rate risk, which is the risk of losses on the bank's positions in foreign currency because of changes in exchange rates.
- Investment price risk, which is the risk of losses because of changes in investments prices.

Notes to the Financial Statements

For the Year Ended 31 December 2009

4 Financial Risk Management (continued)

4.5 Market risk (continued)

4.5.1 Interest rate risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates. The bank's operations are subject to the risk of interest rate fluctuations to the extent that interest-earning assets and interest-bearing liabilities mature or re-price at different times or at different amounts. The bank accepts deposits from customers at both fixed and floating rates and for varying maturity periods. This risk is managed through the matching of the interest resetting dates on assets and liabilities. However, the bank seeks to maximise the spread over the cost of capital by investing funds in a portfolio of securities and loans and receivables with a longer tenure than the liabilities (therefore carrying a negative maturity gap position) through the efficient management of shorter term liabilities over the medium to longer term. The table below summarises re-pricing mismatches at balance sheet date together with the effective interest rates where applicable.

2009	EUR	Effective Interest Rate %	Less than three months EUR	Between three months and one year EUR	Between one year and five years EUR	More than five years EUR	Others EUR
Assets							
Cash	850	-	850	-	-	-	-
Balances with Central Bank of Malta	504,998	1.3	504,998	-	-	-	-
Investments:							
- Debt securities							
held-to-maturity	28,942,299	6.0	14,624,558	14,317,741	-	-	-
- Equities available-for-sale	3,653	-	-	-	-	-	3,653
Loans and advances to banks	11,219,096	1.3	11,219,096	-	-	-	-
Loans and advances to customers	21,140,261	3.0	18,140,261	-	3,000,000	-	-
Factored receivables	5,338,919	-	5,129,781	209,138	-	-	-
Other assets	3,322,579	-	-	-	-	-	3,322,579
Total assets	70,472,655		49,619,544	14,526,879	3,000,000	-	3,326,232
Liabilities							
Balance with Central Bank of Malta	1,500,000	1.0	-	1,500,000	-	-	-
Amounts owed to customers	53,915,259	2.1	25,279,029	12,886,230	15,750,000	-	-
Current tax payable	230,043	-	-	-	-	-	230,043
Other liabilities	1,233,176	-	-	-	-	-	1,233,176
	56,878,478		25,279,029	14,386,230	15,750,000	-	1,463,219
Equity							
Issued capital	4,000,000	-	-	-	-	-	4,000,000
Property revaluation reserve	640,483	-	-	-	-	-	640,483
Depositors compensation scheme reserve	51,417	-	-	-	-	-	51,417
Retained earnings	1,453,095	-	-	-	-	-	1,453,095
Capital contribution	7,449,182	-	-	-	-	-	7,449,182
	13,594,177		-	-	-	-	13,594,177
Total liabilities and equity	70,472,655		25,279,029	14,386,230	15,750,000	-	15,057,396
Gap			24,340,515	140,649	(12,750,000)	-	(11,731,164)
Cumulative Gap			24,340,515	24,481,164	11,731,164	11,731,164	-

Notes to the Financial Statements

For the Year Ended 31 December 2009

4 Financial Risk Management (continued)

4.5 Market risk (continued)

4.5.1 Interest rate risk (continued)

2008	EUR	Effective Interest Rate %	Less than three months EUR	Between three months and one year EUR	Between one year and five years EUR	More than five years EUR	Others EUR
Assets							
Cash	779	-	779	-	-	-	-
Balances with Central Bank of Malta	385,852	2.5	385,852	-	-	-	-
Investments:							
- Debt securities held-to-maturity	26,304,231	6.7	1,635,000	12,716,574	11,952,657	-	-
- Equities available-for-sale	3,653	-	-	-	-	-	3,653
Loans and advances to banks	9,788,398	3.4	9,788,398	-	-	-	-
Loans and advances to customers	15,030,861	4.9	12,030,861	3,000,000	-	-	-
Factored receivables	4,362,518	-	4,362,518	-	-	-	-
Other assets	3,433,785	-	-	-	-	-	3,433,785
Total assets	59,310,077		28,203,408	15,716,574	11,952,657	-	3,437,438
Liabilities							
Amounts owed to customers	45,196,148	3.1	32,964,977	90,000	12,141,171	-	-
Current tax payable	228,666	-	-	-	-	-	228,666
Other liabilities	2,138,538	-	-	-	-	-	2,138,538
	47,563,352		32,964,977	90,000	12,141,171	-	2,367,204
Equity							
Issued capital	4,000,000	-	-	-	-	-	4,000,000
Property revaluation reserve	647,695	-	-	-	-	-	647,695
Retained earnings	7,099,030	-	-	-	-	-	7,099,030
	11,746,725		-	-	-	-	11,746,725
Total liabilities and equity	59,310,077		32,964,977	90,000	12,141,171	-	14,113,929
Gap			(4,761,569)	15,626,574	(188,514)	-	(10,676,491)
Cumulative Gap			(4,761,569)	10,865,005	10,676,491	10,676,491	-

Notes to the Financial Statements

For the Year Ended 31 December 2009

4 Financial Risk Management (continued)

4.5 Market risk (continued)

4.5.1.1 Interest rate profile

At the reporting date the interest rate profile of the bank's interest bearing financial instruments was:

	2009	2008
	EUR	EUR
Fixed rate instruments		
Investments – Debt securities held-to-maturity	14,580,725	11,952,657
Loans and advances to banks	7,031,287	6,761,350
Loans and advances to customers	18,140,261	12,030,861
Balance with Central Bank of Malta	(1,500,000)	-
Amounts owed to customers	(32,633,536)	(31,011,171)
	<u>5,618,737</u>	<u>(266,303)</u>
Variable rate instruments		
Balances with Central Bank of Malta	504,998	385,852
Investments – Debt securities held-to-maturity	14,361,574	14,351,574
Loans and advances to banks	4,187,808	3,027,048
Loans and advances to customers	3,000,000	3,000,000
Amounts owed to customers	(21,281,723)	(14,184,977)
	<u>772,657</u>	<u>6,579,497</u>

4.5.1.2 Fair value sensitivity analysis for fixed rate instruments

The bank does not account for any fixed rate financial assets and liabilities at fair value through profit or loss. Therefore, a change in interest rates at the reporting date would not affect profit or loss.

4.5.1.3 Cash flow sensitivity analysis for variable rate instruments

The sensitivity of the interest rate gaps to various interest rate scenarios is also monitored by management. Standard scenarios that are considered on a monthly basis include a 100 basis point (bp) parallel rise or fall in all the yield curves. An analysis of the bank's sensitivity to an increase or decrease in market interest rates is as presented below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant.

	Impact on profit or loss and equity	
	2009	2008
	EUR	EUR
+100 basis points	7,727	65,795
-100 basis points	(7,727)	(65,795)

Notes to the Financial Statements

For the Year Ended 31 December 2009

4 Financial Risk Management (continued)

4.5 Market risk (continued)

4.5.2 Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to the changes in foreign exchange rates. The bank holds and deals in foreign currency with the aim to service client foreign exchange buying and selling activity. The bank does not speculate on its foreign exchange holdings. The bank's foreign exchange exposure is mainly limited to the United States Dollar and Swiss Francs originating from the bank's corporate banking business. The bank manages this risk by ensuring that its foreign currency denominated liabilities is matched with corresponding assets in the same currency.

Exposure to foreign currencies is maintained at minimum levels and within the prescribed limits set by the bank's Board of Directors. Under the scenario that all foreign currencies fluctuate up or down by 20% against the Euro, the fair values of financial assets and liabilities would fluctuate, up or down by EUR5,196 respectively.

The following table provides an analysis of the financial assets and liabilities of the bank into relevant currency groupings.

	2009			2008		
	Euro EUR	Other Currencies EUR	Total EUR	Euro EUR	Other Currencies EUR	Total EUR
Financial Assets						
Cash	850	-	850	779	-	779
Investments:						
- Debt securities held-to-maturity	28,942,299	-	28,942,299	26,304,231	-	26,304,231
- Equities available-for-sale	3,653	-	3,653	3,653	-	3,653
Loans and advances to banks and balance with Central Bank of Malta	9,025,002	2,699,092	11,724,094	7,624,961	2,549,289	10,174,250
Loans and advances to customers and credit cards	21,140,261	-	21,140,261	15,030,861	-	15,030,861
Factored receivables - Gross	5,393,564	-	5,393,564	4,409,380	-	4,409,380
	64,505,629	2,699,092	67,204,721	53,373,865	2,549,289	55,923,154
Financial liabilities						
Balances with Central Bank of Malta	1,500,000	-	1,500,000	-	-	-
Amounts owed to customers	51,326,002	2,589,257	53,915,259	42,784,096	2,412,052	45,196,148
	52,826,002	2,589,257	55,415,259	42,784,096	2,412,052	45,196,148

At the balance sheet date, the bank was not exposed to any off balance sheet currency risk.

Notes to the Financial Statements

For the Year Ended 31 December 2009

4 Financial Risk Management (continued)

4.5 Market risk (continued)

4.5.3 Investment price risk

The exposure of the bank to this risk is not significant. Frequent management reviews are carried out to ensure high quality of the portfolio.

Fair value and price verification control

The majority of the financial assets and liabilities of the bank are carried at cost or amortised cost and not fair value.

Investments – Debt securities held-to-maturity

This category of assets is carried at amortised cost. The instruments are unquoted and no quoted market price for similar instruments is available. There is no other appropriate or workable method of reasonably estimating the fair value of these unquoted investments for disclosure purposes.

Investments – Equity instruments available-for-sale

The bank has an interest in an unquoted equity investment as disclosed in note 13.3. The investment is measured at fair value. Fair value has been determined by reference to the amount recoverable which is represented by the notional amount of the investment.

Loans and advances to banks and customers and factored receivables

This category of assets is reported net of impairment allowances to reflect the estimated recoverable amounts. 99% of loans and advances to banks are repriceable within 3 months while 1% are repriceable between 3 months and one year. 86% of loans and advances to customers are repriceable within 3 months while 14% are repriceable within two years. 96% of factored receivables are repriceable within 3 months, while 4% are repriceable between 3 months and 1 year. The fact that the majority of this category of financial assets has a short term contractual repricing coupled with the fact that interest rates reflect current market rates, the carrying amounts of these financial assets approximate their fair values.

Amounts owed to customers

This category of liabilities is carried at amortised cost and amounts to €53,915,259 (2008: EUR45,196,148). 47% of the bank's amounts owed to customers have a contractual repricing term of three months or less. The carrying value of these amounts approximates their fair values. In respect of other longer-term fixed-maturity deposits, that are repriceable upon their contractual maturity date, it is not practicable to determine fair value with sufficient reliability. Fair value is therefore taken to be the amount payable at balance sheet date.

Balance with Central Bank of Malta

The loan contracted by the bank for a one year term with the Central Bank of Malta is carried at amortised cost.

Notes to the Financial Statements

For the Year Ended 31 December 2009

4 Financial Risk Management (continued)

4.6 Liquidity risk

Liquidity risk is the risk that the bank's obligations to repay liabilities or fund new loans exceeds the bank's ability to raise funds from either the liquidation of assets or the acceptance of new deposits. Liquidity risk arises because a bank does not exactly match the maturity of assets with the maturity of liabilities but must always be able to meet its liabilities as they fall due. Liquidity risk may also be affected by the depth of the market in which a bank has its assets and liabilities.

The bank's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the bank's reputation.

The bank's liquidity risk management focuses on structuring both the asset and liability portfolio so as to maintain diversity of funding sources and a spread of asset and liability maturities. It is bank's policy to reduce exposure to liquidity risk by matching, as much as possible, assets and liabilities in different maturity periods. A significant proportion of deposits are pledged, which contributes to the reduction of liquidity risk.

Liquidity policies and procedures are reviewed regularly through internal audit reporting. All liquidity policies are subject to the review and approval of the Board of Directors.

The following table provides an analysis of the financial assets and liabilities of the bank into relevant maturity groupings based on the remaining periods to repayment.

At 31 December 2009	Less than one month EUR	Between one and three months EUR	Between three months and one year EUR	Between one and five years EUR	More than five years EUR	Total EUR
Financial assets						
Investments:						
Debt securities held-to-maturity	-	14,580,725	-	5,616,574	8,745,000	28,942,299
Loans and advances to Banks and balance with Central Bank of Malta	8,816,082	2,908,012	-	-	-	11,724,094
Loans and advances to customers	18,140,261	-	-	3,000,000	-	21,140,261
Factored receivables – gross	2,472,870	2,711,556	209,138	-	-	5,393,564
	<u>29,429,213</u>	<u>20,200,293</u>	<u>209,138</u>	<u>8,616,574</u>	<u>8,745,000</u>	<u>67,200,218</u>
Financial liabilities						
Balance with Central Bank of Malta	-	-	1,500,000	-	-	1,500,000
Amounts owed to customers	25,279,029	-	12,886,230	15,750,000	-	53,915,259
	<u>25,279,029</u>	<u>-</u>	<u>14,386,230</u>	<u>15,750,000</u>	<u>-</u>	<u>55,415,259</u>
At 31 December 2008	Less than one month EUR	Between one and three months EUR	Between three months and one year EUR	Between one and five years EUR	More than five years EUR	Total EUR
Financial assets						
Investments:						
Debt securities held-to- maturity	-	-	4,615,000	12,944,231	8,745,000	26,304,231
Loans and advances to Banks and balance with Central Bank of Malta	9,607,900	566,350	-	-	-	10,174,250
Loans and advances to customers	12,030,861	-	3,000,000	-	-	15,030,861
Factored receivables – gross	404,361	3,200,922	804,097	-	-	4,409,380
	<u>22,043,122</u>	<u>3,767,272</u>	<u>8,419,097</u>	<u>12,944,231</u>	<u>8,745,000</u>	<u>55,918,722</u>
Financial liabilities						
Amounts owed to customers	14,699,977	18,265,000	90,000	12,141,171	-	45,196,148

Notes to the Financial Statements

For the Year Ended 31 December 2009

4 Financial Risk Management (continued)

4.6 Liquidity risk (continued)

4.6.1 Exposure to liquidity risk

The key measure used by the bank for managing liquidity risk is the ratio of net liquid assets to customer deposits. For this purpose net liquid assets are considered as comprising cash and cash equivalents less any deposits from banks and other borrowings and commitments maturing within the next month. This calculation is used to measure the bank's compliance with the liquidity limit established by the Malta Financial Services Authority. Details of the bank's ratio of net liquid assets to deposits at the reporting date and during the reported period are as follows:

	2009	2008
As at 31 December	220 %	241%
Average for the year	179 %	356%
Maximum for the year	338 %	795%
Minimum for the year	83 %	204%

4.6.2 Residual contractual maturities of financial liabilities

The table below shows a maturity analysis for financial liabilities by remaining contractual maturities of undiscounted cash flows.

	Carrying amount EUR	Gross nominal inflow / (outflow) EUR	Less than one month EUR	Between one and three months EUR	Between three months and one year EUR	Between one and five years EUR	More than five years EUR
At 31 December 2009							
Balance with							
Central Bank of Malta	1,500,000	(1,515,333)	-	-	(1,515,333)	-	-
Amounts owed to customers	53,915,259	(53,450,226)	(22,788,750)	-	(14,136,576)	(16,524,900)	-
	55,415,259	(54,965,559)	(22,788,750)	-	(15,651,909)	(16,524,900)	-
At 31 December 2008							
Amounts owed to customers	45,196,148	(47,703,707)	(14,714,077)	(19,509,901)	(93,478)	(13,386,251)	-

Notes to the Financial Statements

For the Year Ended 31 December 2009

4 Financial Risk Management (continued)

4.7 Operational risks

Management of operational risk

The bank's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the bank's reputation with overall cost effectiveness. To manage this risk in an appropriate manner the following policies have been adopted:

- To adopt policies, processes and procedures to control and/or mitigate material operational risks.
- To identify and assess the operational risk inherent in all material products, activities, processes and systems. Before new products, activities, processes and systems are introduced or undertaken, the operational risk inherent in them is subject to adequate assessment.
- To monitor all potential operational risks and material exposures to losses.
- To monitor whether there is motive, means and opportunity, within the overall control environment to commit fraudulent acts.
- To adopt contingency and business continuity plans to ensure ability to operate on an ongoing basis and limit losses in the event of severe business disruption.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management. Periodic internal audit reports are submitted to the bank's Audit Committee.

A financial measurement of this risk is arrived at by the bank for the purpose of allocating risk capital using the Basic Indicator Approach under the Capital Requirements Directive rules. The capital requirement for operational risk under this method was calculated at EUR353,874 as at 31 December 2009 (2008: EUR 319,890).

4.8 Additional Pillar III disclosures

Additional Pillar III disclosures, as required by the Capital Requirements Directive and as set out in Banking Rule BR/07/2009, can be found on the bank's website at <http://www.izolabank.eu>.

5 Interest Receivable and Similar Income

	2009 EUR	2008 EUR
On loans and advances to banks	65,383	365,740
On loans and advances to customers	983,221	1,393,074
	<u>1,048,604</u>	<u>1,758,814</u>

6 Interest Expense

	2009 EUR	2008 EUR
On amounts owed to banks	-	21
On amounts owed to customers	1,261,842	1,928,561
	<u>1,261,842</u>	<u>1,928,582</u>

Notes to the Financial Statements

For the Year Ended 31 December 2009

7 Net Fees and Commission Income

	2009 EUR	2008 EUR
Straight-through processing fees	601,160	617,283
Commissions from factoring services	389,667	247,744
Fees and commission income	990,827	865,027
SWIFT and bank charges	(32,486)	(23,921)
Fees and commission expense	(32,486)	(23,921)
	958,341	841,106

8 Net Trading Gains

Net trading gains comprise exchange rate differences.

9 Impairment Allowances

	2009 EUR	2008 EUR
Write downs		
Factored receivables		
- collective allowances	(7,784)	(17,011)
- bad debts written off	-	(82,020)
	(7,784)	(99,031)
Reversals of write downs		
Factored receivables		
- specific allowances	-	82,020
	(7,784)	(17,011)

10 Profit before Income Tax

10.1 Profit before income tax is stated after charging fees payable to the bank's auditors during 2009 for:

	EUR
Auditors' remuneration	23,364
Tax advisory services	7,200
Other non-audit services	11,256
	41,820

Notes to the Financial Statements

For the Year Ended 31 December 2009

10 Profit before Income Tax (continued)

10.2 Staff costs incurred by the bank during the year are analysed as follows:

	2009 EUR	2008 EUR
Directors' fees	24,261	14,957
Staff costs:		
- wages, salaries and allowances	209,767	192,802
- defined contribution social security costs	10,573	10,206
	<u>244,601</u>	<u>217,965</u>

10.3 The weekly average number of persons employed by the bank during the year was as follows:

	2009 No.	2008 No.
Managerial	3	3
Supervisory and clerical	4	4
	<u>7</u>	<u>7</u>

11 Income Tax Expense

11.1 Total income tax expense

	Note	2009 EUR	2008 EUR
Current tax expense			
Current year		195,923	191,028
Deferred tax expense			
Origination and reversal of temporary differences	20.2	(35,221)	9,638
		<u>160,702</u>	<u>200,666</u>

11.2 The income tax expense for the year and the result of the accounting profit multiplied by the tax rate applicable in Malta, the bank's country of incorporation, are reconciled as follows:

	2009 EUR	2008 EUR
Profit before income tax	1,558,972	1,573,676
Income tax at the applicable tax rate of 35%	(545,640)	(550,787)
Income tax effect of:		
Flat rate foreign tax credit	359,992	356,820
Different tax rates	29,391	(2,465)
Depreciation charges not deductible by way of capital allowances	(2,060)	(1,858)
Non-taxable income	137	137
Non-deductible expenses	(2,522)	(2,513)
Tax expense	<u>(160,702)</u>	<u>(200,666)</u>

Notes to the Financial Statements

For the Year Ended 31 December 2009

12 Earnings per Share

Earnings per share is calculated on the profit after tax of the bank for the year ended 31 December 2009 amounting to EUR1,398,270 (2008: EUR1,373,010) divided by 160,000 (2008: 160,000), being the number of ordinary shares in issue and ranking for dividend during the year.

13 Investments

13.1 Investments comprise:

	2009 EUR	2008 EUR
Debt securities held-to-maturity	28,942,299	26,304,231
Equity instruments available-for-sale	3,653	3,653
	<u>28,945,952</u>	<u>26,307,884</u>

13.2 Debt securities held-to-maturity comprise unquoted non-convertible nominative bonds amounting to EUR27,101,944 (2008: EUR26,304,231) issued by related parties and acquired on issuance by the bank and Malta Government treasury bills amounting to EUR1,840,356. The unquoted non-convertible nominative bonds are cash secured by amounts owed to customers held by the bank. The Malta Government treasury bills are pledged in favour of the Central Bank of Malta to the extent of EUR1,500,000 (2008: Nil).

13.3 Equity instruments available-for-sale comprise:

	2009 EUR	2008 EUR
Unquoted equity holding - Society for Worldwide Interbank Financial Telecommunications SCRL 2 ordinary shares fully paid up	3,653	3,653

13.4 The movement in investments may be summarised as follows:

	Held-to- maturity EUR	Available- for-sale EUR	Total EUR
At 1 January 2008	25,565,225	3,653	25,568,878
Capitalisation of interest	739,006	-	739,006
At 31 December 2008	<u>26,304,231</u>	<u>3,653</u>	<u>26,307,884</u>
At 1 January 2009	26,304,231	3,653	26,307,884
Acquisitions	1,850,356	-	1,850,356
Capitalisation of interest	787,712	-	787,712
At 31 December 2009	<u>28,942,299</u>	<u>3,653</u>	<u>28,945,952</u>

Notes to the Financial Statements

For the Year Ended 31 December 2009

14 Loans and Advances to Banks

	2009 EUR	2008 EUR
Repayable on call and at short notice	1,687,808	3,027,048
Term loans and advances	9,531,288	6,761,350
	<u>11,219,096</u>	<u>9,788,398</u>

15 Factored Receivables

	2009 EUR	2008 EUR
Receivables factored without recourse	5,393,565	4,409,380
Allowance for uncollectibility	(54,646)	(46,862)
	<u>5,338,919</u>	<u>4,362,518</u>

	Collective allowances EUR
At 1 January 2009	46,862
Additions	7,784
At 31 December 2009	<u>54,646</u>

An allowance for uncollectibility is provided against receivables factored without recourse, other than exposures to European governmental agencies.

16 Other Loans and Advances to Customers

16.1 Term loans and advances

	2009 EUR	2008 EUR
	<u>21,140,261</u>	<u>15,030,861</u>

16.2 Loans and advances to customers represent amounts due by related parties.

16.3 Loans and advances to customers amounting to EUR18,717,000 (2008: EUR14,985,000) are cash secured by amounts owed to customers held by the bank and no specific allowance for uncollectibility is necessary.

Notes to the Financial Statements

For the Year Ended 31 December 2009

17 Property and Equipment

	Revalued amount			Cost	
	Total EUR	Premises and improvements EUR	Computer hardware and software EUR	Other equipment EUR	Motor vehicles EUR
Cost/revaluation					
At 1 January 2008	3,280,938	1,611,007	1,343,146	320,962	5,823
Acquisitions	141,712	-	122,957	18,755	-
At 31 December 2008	<u>3,422,650</u>	<u>1,611,007</u>	<u>1,466,103</u>	<u>339,717</u>	<u>5,823</u>
At 1 January 2009	3,422,650	1,611,007	1,466,103	339,717	5,823
Acquisitions	260,725	35,475	205,592	19,658	-
At 31 December 2009	<u>3,683,375</u>	<u>1,646,482</u>	<u>1,671,695</u>	<u>359,375</u>	<u>5,823</u>
Depreciation					
At 1 January 2008	1,174,705	105,122	790,069	277,839	1,675
Charge for the year	238,095	16,407	202,716	17,805	1,167
At 31 December 2008	<u>1,412,800</u>	<u>121,529</u>	<u>992,785</u>	<u>295,644</u>	<u>2,842</u>
At 1 January 2009	1,412,800	121,529	992,785	295,644	2,842
Charge for the year	253,889	17,451	217,311	17,964	1,163
At 31 December 2009	<u>1,666,689</u>	<u>138,980</u>	<u>1,210,096</u>	<u>313,608</u>	<u>4,005</u>
Carrying amount					
At 1 January 2008	<u>2,106,233</u>	<u>1,505,885</u>	<u>553,077</u>	<u>43,123</u>	<u>4,148</u>
At 31 December 2008	<u>2,009,850</u>	<u>1,489,478</u>	<u>473,318</u>	<u>44,073</u>	<u>2,981</u>
At 1 January 2009	<u>2,009,850</u>	<u>1,489,478</u>	<u>473,318</u>	<u>44,073</u>	<u>2,980</u>
At 31 December 2009	<u>2,016,686</u>	<u>1,507,502</u>	<u>461,599</u>	<u>45,767</u>	<u>1,818</u>

There were no capitalised borrowing costs related to the acquisition of property and equipment during the year (2008: Nil).

The carrying amount of premises and improvements that would have been included in the financial statements had these assets been carried at cost less depreciation is EUR485,147 (2008: EUR491,399).

At balance sheet date capital expenditure contracted but not provided for in the accounts amounted to EUR338,444 (2008: EUR221,490).

Notes to the Financial Statements

For the Year Ended 31 December 2009

18 Other Assets

	2009 EUR	2008 EUR
Accrued income	1,010,276	1,234,068
Accounts receivable and prepayments	295,617	189,867
	<u>1,305,893</u>	<u>1,423,935</u>

Accrued income on bonds issued by foreign related parties amounted to EUR1,006,481 (2008: EUR1,232,588).

19 Amounts Owed to Customers

	2009 EUR	2008 EUR
Repayable on demand	23,781,723	14,184,977
Term deposits	30,133,536	31,011,171
	<u>53,915,259</u>	<u>45,196,148</u>

Amounts owed to customers include an amount of EUR43,291,145 (2008: EUR38,111,237) owing by the bank to related parties.

20 Deferred Tax Liabilities

20.1 Deferred income taxes are calculated on all temporary differences under the balance sheet liability method using rates substantively enacted at balance sheet date. The deferred income tax balance composition is as follows:

	Assets 2009 EUR	Liabilities 2009 EUR	Net 2009 EUR	Assets 2008 EUR	Liabilities 2008 EUR	Net 2008 EUR
Excess of capital allowances over depreciation	-	(5,219)	(5,219)	-	(36,147)	(36,147)
Collective impairment allowances	2,868	-	2,868	2,459	-	2,459
Revaluation of property	-	(344,877)	(344,877)	-	(348,761)	(348,761)
	<u>2,868</u>	<u>(350,096)</u>	<u>(347,228)</u>	<u>2,459</u>	<u>(384,908)</u>	<u>(382,449)</u>

Notes to the Financial Statements

For the Year Ended 31 December 2009

20 Deferred Tax Liabilities (continued)

20.2 Movement in temporary differences relating to:

	At 1 January 2009 EUR	Recognised in income EUR	At 31 December 2009 EUR
Excess of capital allowances over depreciation	(36,147)	30,928	(5,219)
Collective impairment allowances	2,459	409	2,868
Revaluation of property	(348,761)	3,884	(344,877)
	<u>(382,449)</u>	<u>35,221</u>	<u>(347,228)</u>

	At 1 January 2008 EUR	Recognised in income EUR	At 31 December 2008 EUR
Excess of capital allowances over depreciation	(26,038)	(10,109)	(36,147)
Collective impairment allowances	1,566	893	2,459
Specific impairment allowances	4,306	(4,306)	-
Revaluation of property	(352,645)	3,884	(348,761)
	<u>(372,811)</u>	<u>(9,638)</u>	<u>(382,449)</u>

21 Accruals and Deferred Income

	2009 EUR	2008 EUR
Accrued interest payable	639,668	1,438,331
Deferred factoring commissions	51,821	45,190
Other accrued expenses	194,459	272,568
	<u>885,948</u>	<u>1,756,089</u>

Accruals and deferred income includes amounts due to related parties amounting to EUR543,388 (2008: EUR784,393).

Notes to the Financial Statements

For the Year Ended 31 December 2009

22 Share Capital and Reserves

22.1 Share capital

	Ordinary shares	
	2009	2008
	No.	No.
On issue at 1 January:		
Issued for cash	54,762	54,762
Issued in lieu of dividend payment	105,238	105,238
On issue at 31 December – fully paid	<u>160,000</u>	<u>160,000</u>

At 31 December 2009, the authorised and issued share capital comprised 160,000 ordinary shares (2008: 160,000) of EUR25 each.

All shares in issue are fully paid up.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at shareholders' meetings of the bank.

22.2 Property revaluation reserve

The property revaluation reserve represents the surplus arising on the revaluation of the bank's premises and improvements, net of related deferred tax effects, and net of that part of the surplus realised through use or disposal of the revalued property. This reserve is not distributable except on realisation of the assets through sale.

22.3 Depositor compensation scheme reserve

The depositor compensation scheme reserve represents amounts set aside by the bank from its retained earnings. This reserve is non-distributable.

22.4 Capital contribution

On 29 December 2009, the bank's shareholders, by virtue of formal Capital Contribution Agreements, contributed an amount of EUR7,449,182 to the distributable reserves of the bank.

22.5 Availability of reserves for distribution

	2009	2008
	EUR	EUR
Distribution	8,902,277	7,099,030
Non-distributable	<u>691,900</u>	<u>647,695</u>
	<u>9,594,177</u>	<u>7,746,725</u>

Notes to the Financial Statements

For the Year Ended 31 December 2009

23 Commitments

	2009 EUR	2008 EUR
Unutilised factoring and credit card commitments	<u>6,835,420</u>	<u>5,917,759</u>

The bank may unconditionally cancel factoring commitments at its discretion, other than amounts being currently utilised by customers.

Factoring commitments are granted to customers at prevailing market rates at transfer date.

24 Net cash generated from/(used in) operations

	2009 EUR	2008 EUR
Profit for the year:	1,398,270	1,373,010
Adjustments for:		
Depreciation	253,889	238,095
Income tax expense	160,702	200,666
Impairment allowance	7,784	17,011
Interest receivable on debt securities	(1,674,301)	(1,770,484)
	<u>146,344</u>	<u>58,298</u>
Working capital changes:		
Loans and advances to banks and customers and factored receivables	(7,014,832)	(2,234,532)
Amounts owed to customers and accruals and deferred income	9,268,645	1,417,182
	<u>2,400,157</u>	<u>(759,052)</u>

25 Cash and cash equivalents

	2009 EUR	2008 EUR
Cash	850	779
Balances with Central Bank of Malta	504,998	385,852
Loans and advances to banks with contractual maturity of three months or less	11,219,096	9,788,398
	<u>11,724,944</u>	<u>10,175,029</u>

Notes to the Financial Statements

For the Year Ended 31 December 2009

26 Operating Leases

The future minimum lease payments for the bank under non-cancellable operating lease rentals payable to a third party are as follows:

	2009 EUR	2008 EUR
Less than one year	11,808	11,808
Between one and five years	14,319	26,127
	<u>26,127</u>	<u>37,935</u>

The bank leases two motor vehicles under operating leases. During the year ended 31 December 2009, EUR11,808 was recognised as an expense in the statement of comprehensive income in respect of operating leases (2008: EUR11,808).

In case of termination of the lease contract, the bank is entitled to pay liquidation damages equivalent to 50% of the rental charges due from the date of termination for the period of all unexpired leases including all rental charges due to the termination of the contract.

27 Related Parties

27.1 Identity of related parties

Related parties are related by virtue of having common directors. Transactions with related parties are carried out entirely on an arm's length basis.

27.2 Related party transactions

Interest, fees and other income/charges in respect of related parties in the statement of comprehensive income comprise:

	2009 EUR	2008 EUR
Interest receivable and similar income	2,631,566	3,155,292
Fees and commissions receivable	954,029	860,899
Other operating income	4,193	4,193
	<u>421,649</u>	<u>1,206,668</u>
Interest expense	421,649	1,206,668

Notes to the Financial Statements

For the Year Ended 31 December 2009

27.3 Related party balances

The statement of financial position includes outstanding transactions and balances in respect of related parties as follows:

	2009	2008
	EUR	EUR
Assets		
Loans and advances to customers	21,140,261	15,030,861
Investments	27,101,943	26,304,231
Prepayments and accrued income	1,006,481	1,232,588
	<u> </u>	<u> </u>
	2009	2008
	EUR	EUR
Liabilities		
Amounts owed to customers	43,291,145	38,111,237
Accruals and deferred income	543,388	784,393
	<u> </u>	<u> </u>

27.4 Compensation to key management personnel

	2009	2008
	EUR	EUR
Compensation to key management personnel	141,503	112,793
	<u> </u>	<u> </u>

27.5 Ultimate controlling party

The financial results and assets and liabilities of the bank are included in the consolidated financial statements of VMKG PLLC, the registered office of which is Bruulstraat 77, 1130 Brussels, Belgium.

28 Operating Segments

The bank has identified one reportable operating segment, being corporate banking services, which is its only strategic business unit. Revenues earned and expenses incurred are the result of corporate banking services provided to its clients. Management does not use any other internal report for decision making which is significantly different from information disclosed in the statements of comprehensive income.

Notes to the Financial Statements

For the Year Ended 31 December 2009

29 Accounting Estimates and Judgements

29.1 The directors considered the development, selection and disclosure of the bank's critical accounting policies and estimates and the application of these policies and estimates. Estimates and judgements are continually evaluated and are based on historical and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

29.2 Critical accounting judgements in applying the bank's accounting policies

Certain critical accounting judgements in applying the bank's accounting policies are described below.

29.2.1 Classification of held-to-maturity investments

The bank follows the guidance in IAS 39 on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. The classification requires significant judgement. In making this judgment, the bank evaluates its intention and ability to hold such investments to maturity. If the bank fails to keep these investments to maturity other than for specific circumstances, for example, selling an insignificant amount close to maturity, it will be required to reclassify the entire class as available-for-sale. The investments would therefore be measured at fair value instead of at amortised cost.

29.2.2 Impairment losses on loans and advances and factored receivables

The bank reviews its loan portfolio to assess impairment on an ongoing basis as relevant generic data is observed concerning risks associated with loans and factored receivables with similar risk characteristics. As a result, the bank makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans and factored receivables, before the decrease is actually identified with an individual loan or factored receivable in that portfolio. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

29.2.3 Revaluation of premises

The bank's premises are measured at revaluation amount less accumulated depreciation. The revaluation amount is determined on the basis of open market values provided periodically, but at least every five years, by independent valuers. The open market valuation provided by independent valuers on 14 August 2007 of the property disclosed in note 17 was EUR1,747,030. The directors applied a downward adjustment of EUR232,937 to limit the revaluation to what they believe is the lower range of the fair open market value.

30 Events after the Balance Sheet Date

Subject to applicable regulatory approval, on 15 February 2010, the Board of Directors approved a base Prospectus for a debt issuance programme for an aggregate of EUR28,000,000 secured bonds and the issuance thereunder of a first tranche of EUR7,000,000 Secured Bonds 2015 subject to an over-allotment option of EUR2,000,000.

31 Comparative Information

Certain comparative amounts have been reclassified to conform with the current year's presentation.



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Independent Auditors' Report

To the shareholders of Izola Bank Limited

Report on the Financial Statements

We have audited the financial statements of Izola Bank Limited (the "bank") as set out on pages 8 to 45 ("the financial statements"), which comprise the statement of financial position as at 31 December 2009 and the statements of comprehensive income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' Responsibility for the Financial Statements

As explained more fully in the Directors' responsibilities statement set out on page 6 of the Directors' report, the directors are responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards as adopted by the EU and the Companies Act, 1995 (Chapter 386, Laws of Malta) (the "Act"). This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. This report, including the opinion, has been prepared for and only for the bank's members as a body in accordance with Article 179 of the Act and Article 31 of the Banking Act, 1994 (Chapter 371, Laws of Malta) and may not be appropriate for any other purpose.

In addition, we read the Director's Report and consider the implications for our report if we become aware of any material misstatement of fact.

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

KPMG, a Maltese civil partnership, is a member firm of KPMG International Cooperative ("KPMG International"), a Swiss entity

The firm is registered as a partnership of Certified Public Accountants in terms of the Accountancy Profession Act.

A list of partners and directors of the firm is available at Portico B Building, Marina Street, Pieta', PTA 9044 Malta.



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Independent Auditors' Report (continued)

To the shareholders of Izola Bank Limited

Report on the Financial Statements (continued)

Opinion on Financial Statements

In our opinion, the financial statements:

- give a true and fair view of the financial position of the bank as at 31 December 2009, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU; and
- have been properly prepared in accordance with the Companies Act, 1995 (Chapter 386, Laws of Malta) and the Banking Act, 1994 (Chapter 371, Laws of Malta).

Report on Other Legal and Regulatory Requirements

Matters on which we are required to report by the Banking Act, 1994 (Chapter 371, Laws of Malta).

In our opinion:

- we have obtained all the information and explanations which, to the best of our knowledge and belief, were necessary for the purpose of our audit;
- proper books of account have been kept by the bank so far as appears from our examination thereof;
- the bank's financial statements are in agreement with the books of account; and
- to the best of our knowledge and belief and, on the basis of the explanations given to us, the financial statements give the information required by law in force in the manner so required.

Matters on which we are required to report by exception by the Companies Act, 1995 (Chapter 386, Laws of Malta) (the "Act"), other than those reported upon above.

We have nothing to report in respect of the following matters where the Act requires us to report to you if, in our opinion:

- the information given in the Chairman's Statement and Directors' Report for the financial year for which the financial statements are prepared is not consistent with the financial statements; or
- certain disclosures of directors' remuneration specified by the Act are not made.

Joseph C Schembri (Partner) for and on behalf of

KPMG

15 February 2010

Registered Auditors

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