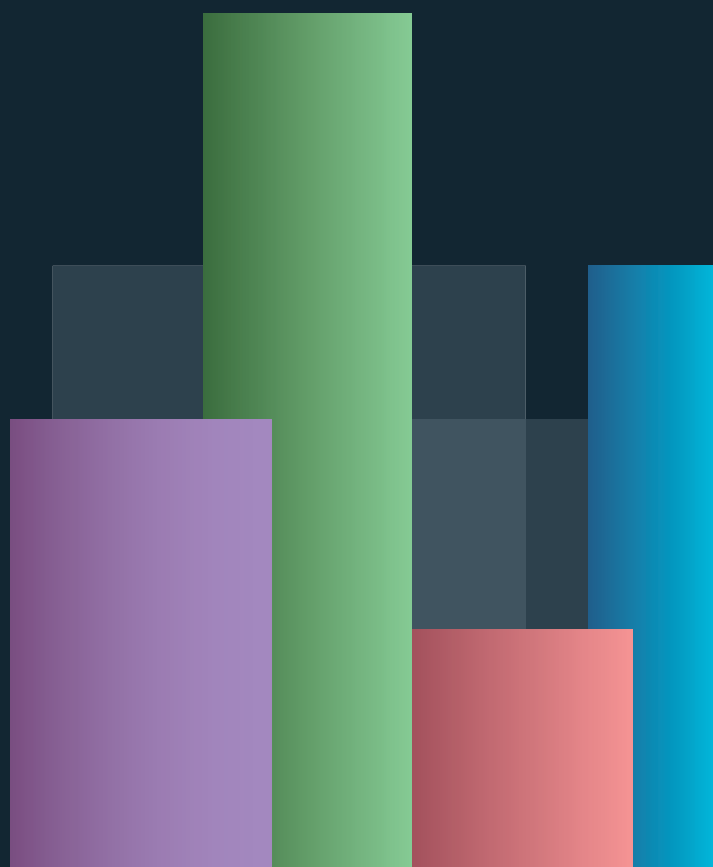




European Bank
for Reconstruction and Development



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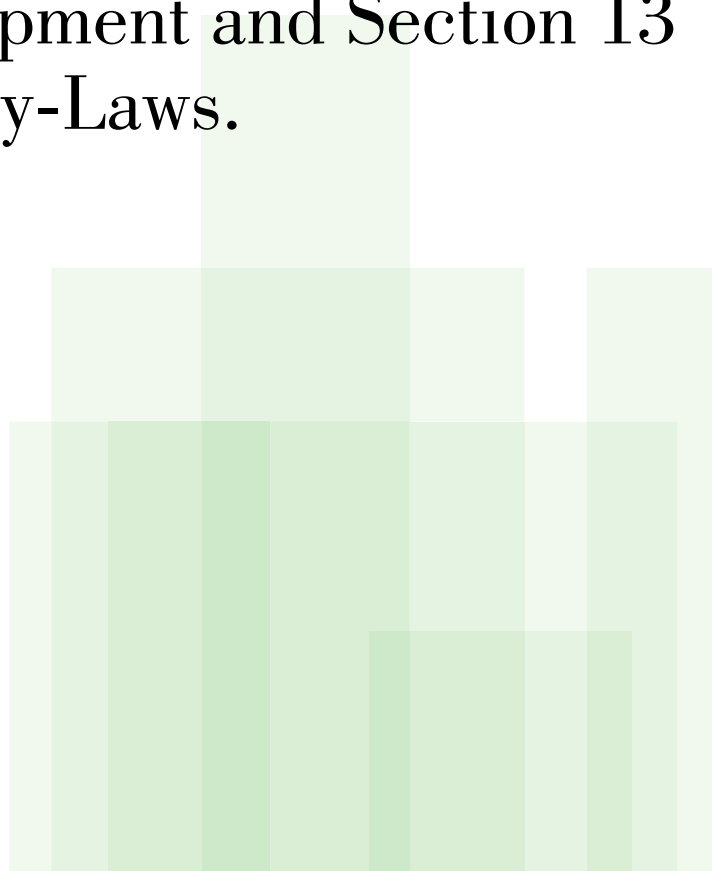
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The EBRD is an international financial institution that supports projects from central Europe to central Asia. Investing primarily in private sector clients whose needs cannot be fully met by the market, the Bank fosters transition towards open and democratic market economies. In all its operations the EBRD follows the highest standards of corporate governance and sustainable development.

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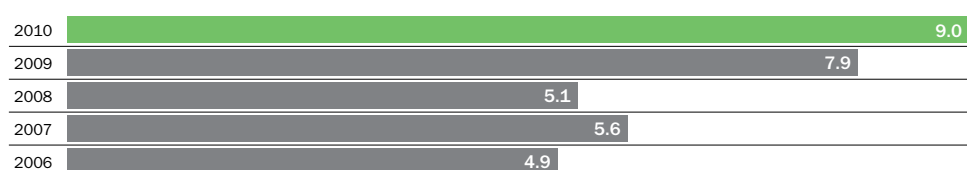
The Financial Report 2010 includes the approved and audited financial statements required to be submitted under Article 27 of the Agreement Establishing the European Bank for Reconstruction and Development and Section 13 of its By-Laws.



Highlights

EBRD commitments 2006-10*

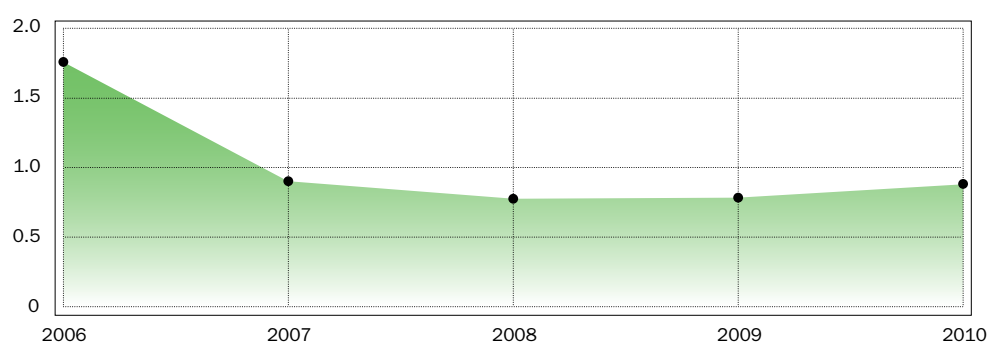
€ billion



*"Commitments" signifies EBRD financing committed under signed agreements.

Realised profit for the year before impairment 2006-10

€ billion



Financial results 2006-10

€ million	2010 ¹	2009	2008	2007	2006
Realised profit for the year before impairment	927	849	849	973	1,691
Net profit/(loss) for the year before transfers of net income approved by the Board of Governors	1,377	(746)	(602)	1,884	2,389
Transfers of net income approved by the Board of Governors	(150)	(165)	(115)	–	–
Net profit/(loss) for the year after transfers of net income approved by the Board of Governors	1,227	(911)	(717)	1,884	2,389
Paid-in capital	6,197	5,198	5,198	5,198	5,198
Reserves and retained earnings	6,780	6,317	6,552	8,676	6,974
Total members' equity	12,977	11,515	11,750	13,874	12,172

Annual investments 2006-10

	2010	2009	2008	2007	2006	Cumulative 1991-2010
Number of projects ²	386	311	302	353	301	3,119
– Stand-alone projects	197	184	161	187	167	1,984
– Investments under frameworks	189	127	141	166	134	1,135
EBRD commitments (€ million) ³	9,009	7,861	5,087	5,583	4,936	61,975
Resources mobilised (€ million) ³	13,174	10,347	8,372	8,617	7,645	115,012
Total project value (€ million) ³	22,039	18,087	12,889	13,809	12,014	178,832

¹ Upon early adoption of IFRS 9 on 1 January 2010, comparatives for 2009 are not required and as such, IFRS 9 has an impact on year-on-year comparisons of the Bank's financial results.

² An operation that is not linked to a framework and involves only one client is referred to as a stand-alone project. Operations extended to a number of clients (for example, credit lines to banks) have a framework which represents the overall amount approved by the Board. Investments under frameworks represent the commitment to individual clients.

³ The calculation of "Resources mobilised" and "Total project value" has been refined to exclude amounts relating to facilities where the original commitment was made in a previous year to ensure the finance is counted only once, whereas "EBRD commitments" include incremental EBRD finance on existing operations.

Financial results

The Bank recorded a net realised profit before Banking loan provisions, unrealised gains on share investments and other unrealised amounts of €927 million, compared with a net realised profit of €849 million recorded in 2009. Including unrealised amounts, the Bank recorded a net profit of €1.4 billion for 2010 before transfers of net income approved by the Board of Governors, compared with a net loss of €746 million for 2009.⁴

The movement in profit mainly reflects an increase in the value of the Bank's share investments holdings and lower loan loss provisions. With increased business volume in 2010, the Bank's total assets reached €39.3 billion at 31 December 2010 (2009: €32.5 billion), a year-on-year increase of more than 20 per cent.

⁴ Upon early adoption of IFRS 9 on 1 January 2010, re-statement of comparatives for 2009 is not required and as such, IFRS 9 has an impact on year-on-year comparisons of the Bank's financial results. For details on the impact of IFRS 9, please refer to the section "A. Basis of preparation – New and amended standards adopted by the Bank" on page 17.

In November 2009 a new accounting standard IFRS 9 Financial Instruments (IFRS 9) was issued with mandatory application from 1 January 2013 with early adoption permitted. The standard was adopted early by the Bank as the new standard better reflects the Bank's business model for managing its financial assets. The impacts to the Bank's financial results were a net gain to the income statement of €301 million and a net increase to reserves of €216 million. The impact of IFRS 9 on the Bank's financial results is further discussed in the "Accounting Policies" section on page 17.

After payment for the increase in paid-in capital of €1.0 billion and transfer to the EBRD Shareholder Special Fund of €150 million, the Bank's reserves were €6.8 billion at the end of 2010 (2009: €6.3 billion). The increase primarily reflects the net profit for the year and the reversal of unrealised losses in reserves of €219 million (relating to Treasury assets) upon adoption of IFRS 9.

The Bank has maintained its strong capital position during the year, with members' equity and callable capital totalling €27.6 billion at 31 December 2010 (2009: €26.1 billion). This compared with Banking risk assets of €21.3 billion at the end of the year (2009: €17.9 billion). Treasury assets of €13.8 billion at 31 December 2010 were of a high credit quality, with 95 per cent being of investment grade quality⁵ (2009: €12.2 billion and 93 per cent). The Bank continues to be able to borrow at favourable rates, maintains high levels of liquidity and enjoys the strong support of its shareholders.

The performance of the Bank's two operating segments, Banking and Treasury, is discussed below.

BANKING OPERATIONS

Annual business volume and portfolio

Reported annual business volume⁶ amounted to €9.0 billion in 2010, comprising 386 projects and 57 outstanding balances under the 2010 Trade Facilitation Programme (2009: €7.9 billion, 311 projects and 58 trade finance balances). This record level of annual business volume reflects the Bank's continued vigorous response to the impact of the global economic crisis on its countries of operations.

Reflecting the Bank's strategic focus, activity levels were strong in the early transition countries (ETC) and the Western Balkans. In the ETC 114 transactions were signed with a record business volume of €920 million. In the Western Balkans region, volume increased by 43 per cent from €727 million in 2009 to over €1.0 billion in 2010. The Bank continued to implement its Sustainable Energy Initiative, and sustainable energy investments reached almost €2.2 billion, up 64 per cent from 2009 and accounting for nearly a quarter of total Bank financing in 2010.

Net cumulative business volume⁷ since the Bank's inception reached €62.0 billion by the end of 2010 (2009: €47.7 billion). Including co-financing and third-party finance, this amounted to a total cumulative project value of €178.8 billion (2009: €147.4 billion). The Bank's portfolio grew from €25.6 billion at the end of 2009 to €30.7 billion at the end of 2010. Reflows were 24 per cent higher than in 2009, reflecting robust repayment levels from the Bank's loan portfolio. The record annual business volume resulted in a portfolio growth of 20 per cent during 2010 compared with 19 per cent in 2009. The portfolio growth rate was also influenced by the strengthening of the US dollar relative to the euro by approximately 7 per cent to a year-end rate of €/1.34 (2009: €/1.44).

Gross disbursements reached a record level of €6.0 billion in 2010, a 10 per cent increase on the 2009 level of €5.5 billion. Reported operating assets exceeded the €20 billion mark for the first time, reaching €21.2 billion at end-2010, up 19 per cent compared with the 2009 level of €17.9 billion. Assets comprised €15.8 billion of disbursed outstanding loans (2009: €13.4 billion) and €5.4 billion of disbursed outstanding share investments at historic cost (2009: €4.5 billion).

The Bank attracted a significant additional amount of co-financing funds in 2010, which reached €5.8 billion (2009: €5.1 billion). The Bank mobilised €2.5 billion from private co-financiers (2009: €2.3 billion) and €3.3 billion from public co-financiers (2009: €2.8 billion), of which €2.3 billion came from international financial institutions (IFIs) (2009: €2.7 billion). In addition, the Bank's activities continued to be strongly supported by donor funding, through both the Special Funds programme and Technical and Investment Cooperation Funds.

Financial performance

Banking operations recorded a net profit of €1.3 billion for 2010 (2009: loss of €878 million). This was mainly due to an increase in the value of the Bank's share investments holdings and lower loan loss provisions.

The contribution from share investments to the Bank's income statement is expected to continue to show significant variability from year to year, given its dependence on the timing of exits and the volatility of equity markets. Exits are mainly linked to the completion of the Bank's transition role in the specific operation and the opportunity, in the market or otherwise, to sell its holding. The volatility of the equity markets is expected to result in further variability in the fair value of the Bank's share investments.

⁵ Equivalent to, or above, an external rating of BBB-/Baa3/BBB- in line with Standard & Poor's/Moody's/Fitch ratings.

⁶ The flow of commitments made by the Bank in the year, less cancellations or sales of such commitments within the same time period.

⁷ This measure includes activity under the Bank's Trade Facilitation Programme that has not previously been reported.

TREASURY OPERATIONS

Portfolio

The value of assets under Treasury management at 31 December 2010 was €13.8 billion (2009: €12.2 billion). This included debt securities of €9.6 billion (2009: €2.5 billion), €3.0 billion of placements with credit institutions (2009: €3.2 billion) and collateralised placements of €1.2 billion (2009: €1.2 billion). In 2009 there were Treasury loans of €5.3 billion which were reclassified to debt securities in 2010 upon adoption of IFRS 9.

Financial performance

Treasury operations reported an operating profit of €119 million in 2010 after the full allocation of expenses and the return on net paid-in capital. This compared with an operating profit of €130 million on an equivalent basis for 2009. The net profit for the year was mainly from balance sheet management activities which amounted to €21 million (2009: €40 million) and gains from debt buy backs of €25 million (2009: €13 million).

CAPITAL

At the 2010 Annual Meeting, the Board of Governors approved an increase to the Bank's authorised capital of €10.0 billion, consisting of €1.0 billion of paid-in shares and €9.0 billion of callable shares. As such the Bank's subscribed capital increased from €19.8 billion to €20.8 billion at 31 December 2010. There will be no further impact to the statement of financial position until 50 per cent of the callable shares have been subscribed.

Paid-in capital totalled €6.2 billion at 31 December 2010 (2009: €5.2 billion), of which €16 million was overdue (2009: €17 million).

RESERVES

The Bank's reserves increased from €6.3 billion at the end of 2009 to €6.8 billion at the end of 2010, primarily reflecting the net profit for the year and the reversal of unrealised losses in reserves on Treasury assets upon adoption of IFRS 9. These increases to reserves were partially offset by the payment for the increase in paid-in capital and the transfer of €150 million to the EBRD Shareholder Special Fund, approved by the Board of Governors at the 2010 Annual Meeting.

Before payment for the increase in paid-in capital and the transfer to the EBRD Shareholder Special Fund, unrestricted general reserves increased by €1.2 billion during the year (2009: decrease of €233 million). This mainly reflected the net realised profit before impairment and the reversal of unrealised losses in reserves (relating to Treasury assets) upon adoption of IFRS 9.

EXPENSES

The Bank continues to focus on budgetary discipline, effective cost controls and a proactive cost-recovery programme. The Bank's general administrative expenses for 2010, including depreciation and amortisation, were €250 million (2009: €237 million). Sterling general administrative expenses for 2010, including depreciation and amortisation, totalled £217 million (2009: £204 million).

OUTLOOK FOR 2011

At the Annual Meeting in May 2010 the Bank's Board of Governors expressed their unanimous support for the approval of the Fourth Capital Resources Review (CRR4) which sets out the Bank's strategy for the period 2011 to 2015. Backed by a strong pipeline of upcoming projects, the Bank aims to maintain a robust level of investments in 2011, the first year of the CRR4 strategy period.

While the Bank is expected to remain profitable in 2011, the Bank's results remain vulnerable to volatility in the financial markets, with the fair value of the Bank's share investments portfolio and the level of specific debt impairment having particular influence on its profits.

Additional reporting and disclosures

CORPORATE GOVERNANCE

The EBRD is committed to the highest standards of corporate governance. Responsibilities and related controls throughout the Bank are properly defined and delineated. Transparency and accountability are integral elements of its corporate governance framework. This structure is further supported by a system of reporting, with information appropriately tailored for, and disseminated to, each level of responsibility within the Bank to enable the system of checks and balances on the Bank's activities to function effectively.

The Bank's governing constituent document is the Agreement Establishing the Bank ("the Agreement"), which states that the institution will have a Board of Governors, a Board of Directors, a President, Vice Presidents, officers and staff.

Board of Governors

All the powers of the Bank are vested in the Board of Governors, which represents the Bank's 63 shareholders. With the exception of certain reserved powers, the Board of Governors has delegated the exercise of its powers to the Board of Directors, while retaining overall authority.

Board of Directors

The Board of Directors comprises 23 Directors and is chaired by the President. Each Director represents one or more shareholders. Subject to the Board of Governors' overall authority, the Board of Directors is responsible for the direction of the Bank's general operations and policies. It exercises the powers expressly assigned to it by the Agreement and those powers delegated to it by the Board of Governors.

Board Committees

The Board of Directors has established three Board Committees to assist with its work:

The **Audit Committee** assists the Board of Directors in fulfilling its responsibilities in relation to the following:

- the integrity of the Bank's financial statements and its accounting, financial reporting and disclosure policies and practices
- the soundness of the Bank's systems of internal controls that management has established regarding finance and accounting matters and their effective implementation
- the status, the ability to perform duties independently and the performance of the Bank's compliance, internal audit, evaluation and risk management functions
- the independence, qualifications and performance of the Bank's external auditor
- other responsibilities within its remit.

The **Budget and Administrative Affairs Committee** assists the Board of Directors in fulfilling its responsibilities in relation to the following:

- the budgetary, staff and administrative resources of the Bank
- efficiency, cost control and budgetary prudence
- overseeing the EBRD Shareholder Special Fund, the use of donor funding and relations with the donor community
- the Bank's Human Resources policies
- specific responsibilities in relation to Governors, the President, Vice Presidents and Directors of the Bank
- policies relating to governance and ethics
- the Bank's administrative arrangements
- other responsibilities within its remit.

The **Financial and Operations Policies Committee** assists the Board of Directors in fulfilling its responsibilities in relation to the following:

- the Bank's financial policies
- the Bank's Treasury operations, Liquidity Policy and Borrowing Programme
- the Bank's operational policies
- the Bank's strategic portfolio management within the framework of the Medium Term Strategy
- transparency and accountability of the Bank's operations within the framework of the Public Information Policy and the Project Complaint Mechanism
- other responsibilities within its remit.

The composition of these committees during 2010 is detailed in Chapter 11 of the *Annual Report 2010*.

The President

The President is elected by the Board of Governors. He is the legal representative and chief of staff of the Bank. Under the direction of the Board of Directors, the President conducts the day-to-day business of the Bank.

The President chairs the Bank's Executive Committee, which also includes the Vice Presidents and other members of the Bank's senior management.

Other management committees

Listed below are other management committees that assist the President in the overall management of the Bank.

Management committees	Chair	Purpose of the committee	Meeting frequency
Executive Committee	President	The custodian of all key aspects of the strategy, performance and financial soundness of the Bank.	Weekly
Operations Committee	First Vice President, Banking	Considers all banking transactions at various stages (concept, structure and final reviews) before submission by the President for consideration by the Board of Directors.	Weekly
Equity Committee	First Vice President, Banking	Maintains oversight over listed and unlisted share investments. Reviews and identifies suitable exit opportunities and makes recommendation on such exits to the Operations Committee.	Quarterly
Procurement Complaints Committee	Deputy General Counsel, Banking and Finance	Considers complaints and disputes arising from tendering and contracts for goods, works and consultant services (including those funded by Technical Cooperation funds or the Bank's budget) subject to the Procurement Policies and Rules or the Corporate Procurement Policy, as the case may be. Reviews procurement and related matters referred to it by the Executive Committee.	As necessary
Technical Cooperation Committee	Vice President, Operational Policies	Decides on all transactional and non-transactional Technical Cooperation proposals except those expressly approved by the Board as being subject to an alternative approval process.	Weekly
Information Technology Governance Committee	Vice President, Risk and Resources	Ensures that the Bank's IT strategy and business plan support the Bank's business strategy. Establishes the framework for measuring business benefits and oversees the realisation of benefits arising from IT projects. Reviews and approves business requests for budget allocation on new projects from the approved IT budget.	At least six times per year
Crisis Management Team	Vice President, Finance and Chief Financial Officer	Prepares coordinated response to all critical internal and external issues arising in connection with events that affect the normal operations of the Bank. Ensures that the crisis management plan and business recovery plan is in place and is tested on a regular basis.	At least three times per year
Strategic Human Resources Committee	President	Approves all senior appointments.	As necessary
Enforcement Committee	Deputy General Counsel, Banking and Finance	Oversees the Bank's policies and procedures for processing allegations of fraud, corruption, collusion or coercion in relation to activities and projects financed from the Bank's ordinary capital resources, or from Special Funds, resources or from cooperation funds administered by the Bank. Decides on whether to take any enforcement action based on a third party finding or in implementation of any agreement for the mutual enforcement of debarment decisions in effect between the Bank and another international organisation.	As necessary

EBRD Codes of Conduct

The Codes of Conduct for Officials of the Board of Directors and for Bank Personnel and Experts, approved in May 2006, articulate the values, duties and obligations, as well as the ethical standards that the Bank expects of its Board officials and staff. The Bank has established robust compliance enforcement mechanisms and detailed procedures for investigating allegations of suspected misconduct. The Codes of Conduct also affirm the Bank's commitment to protect whistleblowers.

Compliance

The EBRD has an independent Office of the Chief Compliance Officer (OCCO), which is headed by a Chief Compliance Officer (CCO) reporting directly to the President, and annually, or as

necessary, to the Audit Committee. The CCO can be dismissed by the President only in accordance with guidance given by the Board of Directors in an executive session.

The OCCO's mandate is to promote good governance and ensure the highest standards of integrity are applied throughout all of the activities of the Bank in accordance with international best practice. The responsibilities of the OCCO include dealing with issues of integrity due diligence, confidentiality, conflicts of interest, corporate governance, accountability, ethics, anti-money laundering, counter-terrorist financing and the prevention of fraudulent and corrupt practices. The OCCO is responsible for investigating allegations of fraud, corruption and misconduct.

The OCCO also trains and advises, as necessary, Bank staff members who are appointed as directors to the boards of companies in which the Bank holds an equity interest. Financial and integrity due diligence are integrated into the Bank's normal approval of new business and the monitoring of its existing transactions. The Bank publishes the OCCO's anti-corruption report on its web site.

Moreover, the OCCO has the specific responsibility for administering the Bank's accountability mechanism. This is the Project Complaint Mechanism (PCM), which assesses and reviews complaints about Bank-financed projects and provides, where warranted, a determination as to whether in approving a particular project the Bank acted in compliance with its relevant policies. Within the OCCO there is a dedicated PCM Officer, appointed by the President, who is responsible for day-to-day implementation of the PCM.

During the course of 2010, of note are two particular investigations by the OCCO into allegations of fraud and corruption on the part of one staff member and one Board official. Matters arising out of the first investigation were referred by the Bank to the City of London Police, who initiated an investigation into possible unlawful activities. The referral required certain immunities accorded to the Bank and the staff member to be waived in order to facilitate the investigation. In respect of the second matter, the Bank agreed, in early 2011, to waive the immunities of the Board official and certain other members of the same constituency office assigned to the Bank by a shareholder government, upon requests from the Foreign and Commonwealth Office of the United Kingdom and the authorities of the shareholder government.

Following the first investigation a task force on prohibited practices, chaired by an outside expert and coordinated by the EBRD's Internal Auditor, was mandated to review and, as necessary, make recommendations aimed at strengthening internal procedures and controls. The task force delivered its report in October 2010 and the recommendations are under implementation.

Reporting

The EBRD's corporate governance structure is supported by appropriate financial and management reporting. The Bank has a functioning mechanism to be able to certify in the *Financial Report 2010* as to the effectiveness of internal controls over external financial reporting, using the Committee of Sponsoring Organisations of the Treadway Commission (COSO) internal control framework. This annual certification statement is signed by both the President and the Vice President, Finance and Chief Financial Officer and is subject to a review and an attestation by the Bank's external auditors. In addition, the Bank has a comprehensive system of reporting to its Board of Directors and its committees. This includes reporting to the Audit Committee on the activities of the Evaluation department and the Internal Audit department.

Operational risk

The Bank defines operational risk as all aspects of risk-related exposure other than those falling within the scope of credit, market and liquidity risk. This includes the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events and reputational risk. Examples include:

- errors or failures in transaction support systems and inadequate disaster recovery planning, including errors in the mathematical formulae of pricing or hedging models, or in the computation of the fair value of transactions
- external events
- damage to the Bank's name and reputation, either directly by adverse comments or indirectly
- errors or omissions in the processing and settlement of transactions, whether in the areas of execution, booking or settlement or due to inadequate legal documentation
- errors in the reporting of financial results or failures in controls, such as unidentified limit excesses or unauthorised trading/trading outside policies
- dependency on a limited number of key personnel, inadequate or insufficient staff training or skill levels.

The Bank has a low tolerance for material losses arising from operational risk exposures. Where material operational risks are identified (that is, those that may lead to material loss if not mitigated), appropriate mitigation and control measures are put in place after a careful weighing of the risk/return trade-off. Maintaining the Bank's reputation is of paramount importance and reputational risk has therefore been included in the Bank's definition of operational risk. The Bank will always take all reasonable and practical steps to safeguard its reputation.

Within the Bank, there are policies and procedures in place covering all significant aspects of operational risk. These include first and foremost the Bank's high standards of business ethics and its established system of internal controls, checks and balances and segregation of duties. These are supplemented with:

- the Bank's Codes of Conduct
- disaster recovery/contingency planning
- the Public Information Policy
- client and project integrity due diligence procedures, including anti-money-laundering measures
- procedures for reporting and investigating suspected staff misconduct, including fraud
- the information security framework
- procurement and purchasing policies, including the detection of corrupt practices in procurement.

Responsibility for developing the operational risk framework and for monitoring its implementation resides within the Risk and Resources Vice Presidency. Risk Management is responsible for the overall framework and structure to support line managers who control and manage operational risk as part of their day-to-day activities. Risk Management draft proposals are discussed and reviewed by the Operational Risk Management Group (ORMG), which implements the operational risk management policies and techniques throughout the Bank. The ORMG is chaired by the Vice President, Risk and Resources and its membership comprises senior managers across the Bank who have been identified as potentially facing the most operational risk within their day-to-day activities. The ORMG's task is to develop and coordinate the Bank's approach to managing operational risk, and to ensure that it is widely implemented across all areas of the Bank.

The Bank's current operational risk framework includes an agreed definition (see above); the categorisation of different loss type events to capture the Bank's exposure to operational risk; a group of key risk indicators to measure such risks; the identification of specific operational risks through an annual self-assessment exercise; internal loss data collection; and use of external loss data.

Departments within the EBRD identify their operational risk exposures and evaluate the mitigating controls that help to reduce the inherent or pre-control risk. Each risk (both inherent and post control) is assessed for its impact, according to a defined value scale and the likelihood of occurrence, based on a frequency by time range. Departments also report operational risk incident losses or near misses above €5,000. The intention of collecting such data is primarily to improve the control environment by taking into account the cost of control strengthening and perceived potential future losses. The Bank is a member of GOLD, the external loss database where members "pool" operational risk incident information over a monetary threshold. This provides the Bank with access to a depth of information wider than its own experience and supplements its own analysis on reported internal incidents. GOLD is run as an unincorporated not-for-profit consortium of financial services institutions.

For financial risks, please refer to the Risk Management section on page 28.

External auditors

The external auditors are appointed by the Board of Directors, on the recommendation of the President, for a four-year term. No firm of auditors can serve for more than two consecutive four-year terms. In relation to the 2010 audit, the Bank's auditors, PricewaterhouseCoopers LLP, are in the last year of their second term. The Bank has completed the re-tender of its external audit mandate and Deloitte LLP (UK) has been appointed for the period 2011-14.

The external auditors perform an annual audit to enable them to express an opinion on whether the financial statements present fairly the financial position and the profit of the Bank in accordance with International Financial Reporting Standards. In addition, the external auditors review and offer their opinion on management's assertion as to the effectiveness of internal controls over financial reporting. This opinion is given as a separate report to the audit opinion. At the conclusion of their annual audit, the external auditors prepare a management letter for the Board of Governors, setting out the external auditors' views and management's responses on the effectiveness and efficiency of internal controls and other matters. This letter is reviewed in detail and discussed with the Audit Committee. The Audit Committee reviews the performance and independence of the external auditors annually.

There are key provisions in the Bank's policies regarding the independence of the external auditors. The external auditors are prohibited from providing non-audit related services unless such service is judged to be in the interest of the Bank and unless it is approved by the Audit Committee. However, the external auditors can provide technical cooperation consultancy services relating to client projects; such incidents are reported periodically to the Audit Committee.

COMPENSATION POLICY

The Bank has designed a market-oriented staff compensation policy, within the constraints of the Bank's status as a multilateral institution, to meet the following objectives:

- to be competitive in order to attract and retain high-calibre employees
- to take account of differing levels of responsibility
- to support a climate of constant staff development
- to be sufficiently flexible to respond rapidly to the market
- to motivate and encourage excellent performance.

To help meet these objectives, the Bank's shareholders have agreed that the Bank should use market comparators to evaluate its staff compensation and that salary and performance-based compensation awards should be driven by performance. Market comparators for the Bank are primarily private sector financial institutions in each of its locations plus other IFIs.

The performance-based compensation awards are structured to recognise individual and team contributions to the Bank's overall performance. These payments represent a limited proportion of the overall total compensation and benefits package provided to staff.

EBRD staff remuneration

All staff on fixed-term or regular contracts receive a salary which is reviewed on 1 April each year. In addition, professional members of staff are eligible to receive a performance-based compensation award depending on the Bank's and the individual staff member's performance.

All fixed-term and regular employees, as well as most of the Board of Directors,⁸ the President and Vice Presidents, are covered by medical insurance, participate in the Bank's retirement plans and may be eligible to receive a mortgage subsidy. Professional staff hired from abroad may be eligible for Expatriate/Third Country National status and receive, subject to specific conditions, allowances to assist with relocation, accommodation (to defray the cost of renting or purchasing a home) and the education of their children.

There are two retirement plans in operation; both plans provide a lump sum benefit on leaving the Bank or at retirement age, such that retirement plan obligations to staff once they have left the Bank or retired are minimal (being limited to inflation adjustments on deferred retirement plan benefits under the Final Salary Plan). The Money Purchase Plan is a defined contribution scheme to which both the Bank and staff contribute, with Plan members making individual investment decisions. The Final Salary Plan is a defined benefit scheme, to which only the Bank contributes. The rules for the retirement plans are approved by the Board of Directors and are monitored by a Retirement Plan Committee, a Retirement Plan Administration Committee and a Retirement Plan Investment Committee.

The salaries and emoluments of all staff are subject to an internal tax, applied at rates that vary according to the individual's salary and personal circumstances. Their salaries and emoluments are exempt from national income tax in the United Kingdom.

President and Vice Presidents

The President is elected by the Board of Governors and typically receives a fixed-term contract of four years. His salary and benefits are approved by the Board of Governors. The President can participate in the same benefit schemes as the staff but is not eligible for performance-based compensation awards.

The Vice Presidents are appointed by the Board of Directors on the recommendation of the President and typically have fixed-term contracts of four years. Their salaries and benefits are approved by the Board of Directors. The Vice Presidents can participate in the same benefit schemes as the staff but are not eligible for performance-based compensation awards.

The gross salary, from which internal tax is deducted, for each of these positions is as follows:

	2010 € 000 ⁹	2009 € 000
President	360	346
First Vice President, Banking	319	307
Vice President, Finance and Chief Financial Officer	291	280
Vice President, Risk and Resources	291	280
Vice President, Operational Policies ¹⁰	291	–
Vice President, Environment, Procurement and Administration ¹¹	266	256

Board of Directors

Directors are elected by the Board of Governors for a term of three years and may be re-elected. Directors appoint Alternate Directors. The salaries of Directors and Alternate Directors are approved by the Board of Governors. They can participate in the same benefit schemes as staff but are not eligible for performance-based compensation awards. Some Directors and Alternates are paid directly by the directorship that they represent. In such cases, the funds that would otherwise be used by the Bank to pay such Directors and Alternates are made available to the directorship to offset other eligible costs to the directorship.

The most recently approved gross salaries, from which internal tax is deducted, for these positions are as follows:

	2010 € 000 ⁹	2009 € 000
Director	158	148
Alternate Director	131	122

Senior management

Senior management comprises: members of the Bank's Executive Committee; Director of the President's Office; Managing Directors; Corporate Directors; the Treasurer; the Director, Risk Management; the Controller; the Director of Human Resources; the Head of Internal Audit and the CCO. This group, excluding the President and Vice Presidents (for whom information is given above), consists of 23 individuals who received gross salaries, from which internal tax is deducted, in the range of €118,000 to €223,000⁹ (2009: €113,000 to €214,000) with an average performance-based compensation award of 25 per cent in 2010 (2009: 25 per cent).

⁸ Some Directors and Alternates are paid directly by their constituency and do not participate in the Bank's retirement plans and/or other benefits.

⁹ As salaries are paid in sterling, exchange rates have an impact on year-on-year comparisons.

¹⁰ Employed from 1 September 2010.

¹¹ Employed until 31 August 2010.

Income statement

These financial statements have been approved for issue by the Board of Directors on 15 February 2011.

For the year ended 31 December 2010	Note	Year to 31 December 2010 € million	Year to 31 December 2009 € million
Interest and similar income			
From Banking loans		645	648
From fixed-income debt securities and other interest		131	240
Interest expense and similar charges		(159)	(306)
Net interest income	3	617	582
Net fee and commission income	4	19	14
Dividend income		66	40
Net gains/(losses) from share investments at fair value through profit or loss	5	850	(547)
Net losses from available-for-sale share investments	6	-	(241)
Net losses from loans at fair value through profit or loss	7	(7)	-
Net gains from Treasury assets held at amortised cost	8	10	-
Net losses from Treasury investments	9	-	(9)
Net gains from dealing activities at fair value through profit or loss	10	40	95
Other (losses)/gains	11	(62)	124
Provisions for impairment of Banking loan investments	12	94	(535)
Provisions for impairment of Treasury loan investments	13	-	(32)
General administrative expenses	14	(228)	(220)
Depreciation and amortisation	24,25	(22)	(17)
Net profit/(loss) for the year from continuing operations		1,377	(746)
Transfers of net income approved by the Board of Governors	30	(150)	(165)
Net profit/(loss) after transfers of net income approved by the Board of Governors		1,227	(911)
Attributable to:			
Equity holders		1,227	(911)

Pages 17 to 85 are an integral part of these financial statements.

Statement of comprehensive income

	Year to 31 December 2010 € million	Year to 31 December 2009 € million
For the year ended 31 December 2010		
Net profit/(loss) after transfers of net income approved by the Board of Governors	1,227	(911)
Other comprehensive income/(expense)		
Available-for-sale financial assets	-	635
Share investment designated as fair value through other comprehensive income	(1)	-
Cash flow hedges	15	37
Total comprehensive income/(expense)	1,241	(239)
Attributable to:		
Equity holders	1,241	(239)

Pages 17 to 85 are an integral part of these financial statements.

Statement of financial position

At 31 December 2010	Note	€ million	31 December 2010 € million	€ million	31 December 2009 € million
Assets					
Placements with and advances to credit institutions	15	2,974		3,247	
Debt securities	16				
At fair value through profit or loss		737		222	
At amortised cost		9,065		–	
Less: Provisions for impairment		(110)		–	
Available-for-sale		–		1,012	
Held-to-maturity		–		1,239	
		9,692		2,473	
Collateralised placements	17	1,179		1,171	
			13,845		6,891
Other financial assets	18				
Derivative financial instruments		4,168		2,538	
Other financial assets		525		483	
			4,693		3,021
Loan investments					
Treasury portfolio:	19				
Loans		–		5,484	
Less: Provisions for impairment		–		(163)	
		–		5,321	
Banking portfolio:					
Loans at amortised cost	20	15,243		13,125	
Less: Provisions for impairment	12	(630)		(719)	
Loans at fair value through profit or loss	21	221		–	
		14,834		12,406	
			14,834		17,727
Share investments					
Banking portfolio:	22				
Share investments at fair value through profit or loss		5,798		2,279	
Available-for-sale share investments		–		2,455	
		5,798		4,734	
Treasury portfolio:					
Share investments at fair value through other comprehensive income	23	56		–	
Available-for-sale share investments		–		57	
		56		57	
			5,854		4,791
Intangible assets	24		47		53
Property, technology and office equipment	25		38		39
Paid-in capital receivable			16		17
Total assets			39,327		32,539
Liabilities					
Borrowings					
Amounts owed to credit institutions	26	1,911		2,129	
Debts evidenced by certificates	27	23,036		17,715	
			24,947		19,844
Other financial liabilities	28				
Derivative financial instruments		1,070		803	
Other financial liabilities		333		377	
			1,403		1,180
Total liabilities			26,350		21,024
Members' equity attributable to equity holders					
Paid-in capital	29		6,197		5,198
Reserves and retained earnings	30		6,780		6,317
Total members' equity			12,977		11,515
Total liabilities and members' equity			39,327		32,539
Memorandum items					
Undrawn commitments	31		9,394		7,716

Pages 17 to 85 are an integral part of these financial statements.

Statement of changes in equity

For the year ended 31 December 2010	Subscribed capital € million	Callable capital € million	Available- for-sale revaluation reserve € million	Fair value through other comprehensive income reserve € million	Cash flow reserves € million	Retained earnings € million	Total equity € million
At 31 December 2008	19,794	(14,596)	495	–	(52)	6,109	11,750
Total comprehensive income for the year	–	–	635	–	37	(911)	(239)
Internal tax for the year	–	–	–	–	–	4	4
At 31 December 2009	19,794	(14,596)	1,130	–	(15)	5,202	11,515
Balance at 1 January 2010	19,794	(14,596)	1,130	–	(15)	5,202	11,515
Effect of change in accounting policy for classification and measurement of financial assets (Note 30)	–	–	(1,130)	9	–	1,337	216
Adjusted balance at 1 January 2010	19,794	(14,596)	–	9	(15)	6,539	11,731
Total comprehensive income for the year	–	–	–	(1)	15	1,227	1,241
Internal tax for the year	–	–	–	–	–	5	5
Issuance of paid-in shares	999	–	–	–	–	(999)	–
At 31 December 2010	20,793	(14,596)	–	8	–	6,772	12,977

Refer to Note 30, “Reserves and retained earnings”, on page 77 for a further explanation of the Bank’s reserves.

Pages 17 to 85 are an integral part of these financial statements.

Statement of cash flows¹²

	Year to 31 December 2010		Restated ¹⁴ Year to 31 December 2009
	€ million	€ million	€ million
For the year ended 31 December 2010			
Cash flows from operating activities			
Net profit/(loss) for the year ¹³	1,227		(911)
Adjustments for:			
Unwinding of the discount relating to impaired identified assets	(7)		(3)
Interest income	(769)		(888)
Interest expenses and similar charges	159		306
Net deferral of fees and direct costs	102		108
Realised gains on share investments and equity derivatives	(338)		(98)
Unrealised (gains)/losses on share investments and equity derivatives at fair value through profit or loss	(512)		630
Impairment losses on available-for-sale share investments	-		256
Realised losses on available-for-sale debt securities	-		3
Unrealised losses/(gains) on dealing securities	104		(11)
Fair value movement on hedges	62		(123)
Unrealised mark-to-market movement	387		(97)
Foreign exchange gains	-		(1)
Depreciation and amortisation	22		17
Provisions for impairment of Treasury loan investments and debt securities	(10)		32
Gross provisions (release)/charge for Banking loan losses	(94)		535
	333		(245)
Interest income received	742		974
Interest expenses and similar charges paid	(145)		(328)
(Increase)/decrease in operating assets:			
Prepaid expenses	(79)		(231)
Proceeds from repayments of Banking loans	3,126		3,165
Proceeds from prepayments of Banking loans	1,050		461
Funds advanced for Banking loans	(6,563)		(6,090)
Proceeds from sale of Banking share investments and equity derivatives	759		297
Funds advanced for Banking share investments	(928)		(810)
Net placements to credit institutions	350		746
Movement in amounts owed to credit institutions	(219)		(12)
Increase in operating liabilities:			
Accrued expenses	16		73
Net cash used in operating activities		(1,558)	(2,000)
Cash flows used in investing activities			
Proceeds from repayments of Treasury loans	-		411
Proceeds from sale of available-for-sale debt securities	-		2,393
Purchases of available-for-sale debt securities	-		(1,635)
Proceeds from the redemption of held-to-maturity debt securities	-		2,325
Purchases of held-to-maturity debt securities	-		(2,823)
Proceeds from debt securities at amortised cost	6,068		-
Purchases of debt securities at amortised cost	(7,524)		-
Proceeds from sale of debt securities held at fair value through profit or loss	1,177		878
Purchases of debt securities held at fair value through profit or loss	(1,165)		(52)
Purchases of intangible assets, property, technology and office equipment	(15)		(20)
Net cash (used in)/from investing activities		(1,459)	1,477
Cash flows from financing activities			
Capital received	3		30
Issue of debts evidenced by certificates	15,410		10,644
Redemption of debts evidenced by certificates	(12,312)		(9,494)
Net cash from financing activities		3,101	1,180
Net increase in cash and cash equivalents		84	657
Cash and cash equivalents at beginning of the year		3,232	2,575
Cash and cash equivalents at 31 December		3,316	3,232
Cash and cash equivalents comprise the following amounts with less than three months maturity		2010	2009
		€ million	€ million
Placements with and advances to credit institutions		2,974	3,232
Collateralised placements		342	-
Cash and cash equivalents at 31 December		3,316	3,232

Pages 17 to 85 are an integral part of these financial statements.

¹² The cash flows statement has been prepared using the indirect method. There was a non-cash financing activity in the form of an increase in paid-in capital of €1.0 billion. This amount was transferred from the Bank's reserves (see Note 30).

¹³ Operating profit included dividends of €66 million received for the year to 31 December 2010 (2009: €40 million).

¹⁴ Amounts owed to credit institutions are not considered to be "cash and cash equivalents" in accordance with IAS 7. In prior periods, amounts owed to credit institutions were deducted from "cash and cash equivalents". In light of this, the opening "cash and cash equivalents" amount has been restated for the comparative period. This restatement amounted to an increase in the "cash and cash equivalents" opening balance of €2.1 billion, changing the opening balance previously disclosed of €434 million to €2.5 billion. The comparative period has also been restated for a decrease in net cash used in operating activities of €12 million due to changes in amounts owed to credit institutions. These restatements resulted in the closing "cash and cash equivalents" balance increasing by €2.1 billion in 2009 from €1.1 billion to €3.2 billion. There is no impact to the income statement or the statement of financial position from this restatement.

Accounting policies

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

A. BASIS OF PREPARATION

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB). The financial statements have been prepared under the historical cost convention, as modified by the revaluation of available-for-sale financial assets, financial assets at fair value through other comprehensive income, financial assets and financial liabilities held at fair value through profit or loss and all derivative contracts. In addition, financial assets and liabilities subject to amortised cost measurement, where they form part of a qualifying hedge relationship, have been accounted for in accordance with hedge accounting rules – see “Derivative financial instruments and hedge accounting” on page 20. The financial statements have been prepared on a going concern basis. The going concern assessment takes into account the Bank’s capital adequacy (see the “Capital management” section on page 50), liquidity (see the “Liquidity risk” section on page 45) and other factors.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Bank’s policies. The areas involving a higher degree of judgement or complexity, or areas where judgements and estimates are significant to the financial statements, are disclosed in “Critical accounting estimates and judgements” on page 26.

New and amended standards adopted by the Bank

The following standards, amendments to published standards and interpretations relevant to the Bank were adopted by the Bank in the current year:

IFRS 9, Financial Instruments: Classification and Measurement, was issued in November 2009 with mandatory application from 1 January 2013 with early adoption permitted. The Bank decided to adopt IFRS 9 early, as well as the related amendments to other IFRSs, because the new accounting standard better reflects the Bank’s business model for managing such assets. The Bank chose 1 January 2010 as the date of initial application of IFRS 9. In accordance with the transition provisions of the standard, comparative figures have not been restated.

IFRS 9 replaces the parts of IAS 39 that relate to the classification and measurement of financial assets. It requires financial assets to be classified, at the point of initial recognition, into two measurement categories: those measured at fair value and those measured at amortised cost. The classification depends on both the entity’s business model for managing the assets and their contractual cash flow characteristics.

The main effects resulting from an assessment of the financial assets held by the Bank at the date of initial application of IFRS 9 are shown in the table below and further detailed in the section “Classification of financial assets at the date of initial application of IFRS 9” on page 53.

Financial assets	IAS 39 carrying amount € million	Classification differences € million	Measurement differences € million	IFRS 9 carrying amount € million
Placements with and advances to credit institutions	3,247	–	–	3,247
Debt securities	2,473	5,321	202	7,996
Collateralised placements	1,171	–	–	1,171
Derivative financial instruments	2,538	136	14	2,688
Other financial assets	483	–	–	483
Banking loan investments	12,406	(438)	–	11,968
Treasury loan investments	5,321	(5,321)	–	–
Banking share investments	4,734	302	–	5,036
Treasury share investments	57	–	–	57
Paid-in capital receivable	17	–	–	17
Total financial assets	32,447	–	216	32,663

IAS 27 (Revised), Consolidated and Separate Financial Statements, is effective for accounting periods beginning on or after 1 July 2009. It reduces the alternatives in accounting for subsidiaries in consolidated financial statements and in accounting for subsidiaries in the separate financial statements of a parent, venturer or investor. The standard specifies the circumstances in which an entity must consolidate the financial statements of a subsidiary; the accounting for the changes in the level of ownership interest in a subsidiary; the accounting for the loss of control of a subsidiary; and the information that an entity must disclose to enable users of the financial statements to evaluate the nature of the relationship between the entity and its subsidiary. The adoption of this standard has not had an impact on the Bank's financial statements.

IAS 39 (Amendment), Eligible Hedged Items, is effective for accounting periods beginning on or after 1 July 2009. It clarifies the application of existing principles that determine whether specific risks or portions of cash flows are eligible for designation in a hedging relationship. The Bank applied IAS 39 (Amendment) from its accounting period beginning 1 January 2010. However, based on its existing hedging relationships, the Bank does not consider that the amendment had an impact on its financial statements.

A number of existing standards were revised by the IASB in April 2009 as part of the IFRS improvements project. The following amendments are relevant to the Bank, but they do not have a significant impact on the Bank's financial statements:

- IFRS 8, Operating Segments (effective for accounting periods beginning on or after 1 January 2010)
- IAS 1, Presentation of Financial Statements (effective for accounting periods beginning on or after 1 January 2010)
- IAS 7, Statement of Cash Flows (effective for accounting periods beginning on or after 1 January 2010)
- IAS 17, Leases (effective for accounting periods beginning on or after 1 January 2010)
- IAS 36, Impairment of Assets (effective for accounting periods beginning on or after 1 January 2010)
- IAS 38, Intangible Assets (effective for accounting periods beginning on or after 1 July 2009)
- IAS 39, Financial Instruments: Recognition and Measurement (effective for accounting periods beginning on or after 1 January 2010)
- IFRIC 9, Reassessment of Embedded Derivatives (effective for accounting periods beginning on or after 1 July 2009).

Standards, amendments to published standards and interpretations that are not yet effective and have not been adopted early by the Bank

The following standards, amendments to published standards and interpretations are mandatory for the Bank's accounting periods beginning on or after 1 January 2011 or later periods, and the Bank has not adopted them early:

Pronouncement	Nature of change	IASB effective date
IFRS 7 (Amendment): Financial Instruments: Disclosures – Transfers of Financial Assets	The standard requires disclosure of information that will assist in understanding the relationship between transferred financial assets that are not derecognised in their entirety and the associated liabilities; as well as information that will assist in the evaluation of the nature of, and risks associated with, the entity's continuing involvement in derecognised financial assets. The Bank's initial interpretation is that it will not have a significant impact on its financial statements.	Accounting periods beginning on or after 1 July 2011
IFRS 9 (Reissued): Financial Instruments	The reissued standard maintains the two measurement classifications of amortised cost and fair value through profit or loss for financial liabilities. The standard also clarifies that the changes in fair value due to own credit risk for financial liabilities measured at fair value through profit or loss, are to be presented in other comprehensive income. The Bank's initial interpretation is that it will not have a significant impact on its financial statements.	Accounting periods beginning on or after 1 January 2013
IAS 24 (Revised): Related Party Disclosures	The standard simplifies the definition of related party and provides partial exemption from the disclosure requirements for government-related entities. The Bank's initial interpretation is that it will not have a significant impact on its financial statements.	Accounting periods beginning on or after 1 January 2011
IFRIC 14 (Amendment): Prepayments of a Minimum Funding Requirement	The amendment clarifies the treatment of early payment contributions in circumstances where an entity is subject to minimum funding requirements. The amendment permits such an entity to treat such early payment as an asset. The Bank's initial interpretation is that it will not have a significant impact on its financial statements.	Accounting periods beginning on or after 1 January 2011

A number of existing standards were revised by the IASB in May 2010 as part of the IFRS improvements project. The following amendments are relevant to the Bank, but they do not have a significant impact on the Bank's financial statements:

- IFRS 7, Financial Instruments: Disclosures (effective for accounting periods beginning on or after 1 January 2011)
- IAS 1, Presentation Financial Statements (effective for accounting periods beginning on or after 1 January 2011)
- IAS 27, Consolidated and Separate Financial Statements (effective for accounting periods beginning on or after 1 July 2010)
- IAS 34, Interim Financial Reporting (effective for accounting periods beginning on or after 1 January 2010).

B. SIGNIFICANT ACCOUNTING POLICIES

Financial assets – Classification from 1 January 2010

From 1 January 2010, the Bank classifies its financial assets in the following categories: those measured at amortised cost, and those measured at fair value. This classification depends on both the contractual characteristics of the assets and the business model adopted for their management.

Financial assets at amortised cost

An investment is classified as “amortised cost” only if both of the following criteria are met: the objective of the Bank's business model is to hold the asset to collect the contractual cash flow; and the contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal outstanding, interest being consideration for the time value of money and the credit risk associated with the principal amount outstanding.

Investments meeting these criteria are initially measured at fair value plus transaction costs that are directly attributable to the acquisition of the financial assets. They are subsequently measured at amortised cost using the effective interest method less any impairment. Except for debt securities held at amortised cost which are recognised on trade date, the Bank's financial assets at amortised cost are recognised at settlement date.

Collateralised placements are carried at amortised cost. These are structures wherein the risks and rewards associated with the ownership of a reference asset are transferred to another party through the use of a “total return” swap contract, and are a form of collateralised lending.

Financial assets at fair value

If either of the two criteria above is not met, the debt instrument is classified as “fair value through profit or loss”. The presence of an embedded derivative, which could potentially change the cash flows arising on a debt instrument so that they no longer represent solely payments of principal and interest, will require that instrument to be classified at fair value through profit or loss, an example being a convertible loan.

The Bank's share investments, such as equity investments and derivative instruments, are measured at fair value through profit or loss except for non-trading equity investments designated to be measured at fair value through other comprehensive income. The Bank classifies an investment to be an “equity instrument” if it meets the definition of IAS 32 Financial Instruments: Presentation.

The Bank designates associate share investments and high-risk equity funds at fair value through profit or loss upon initial recognition using the IAS 28 “venture capital” exemption, as the Bank considers these to be venture capital investments. Such assets are carried at fair value on the statement of financial position with changes in fair value included in the income statement in the period in which they occur. The basis of fair value for listed share investments in an active market is the quoted bid market price on the statement of financial position date. The basis of fair value for share investments that are either unlisted or listed in an inactive market is determined using valuation techniques appropriate to the market and industry of each investment. The primary valuation techniques used are net asset value and earnings-based valuations using comparable information and discounted cash flows. Techniques used to support these valuations include industry valuation benchmarks and recent transaction prices.

At initial recognition, the Bank measures these assets at their fair value. Transaction costs of financial assets carried at fair value through profit or loss are expensed in the income statement. Such assets are carried at fair value on the statement of financial position with changes in fair value included in the income statement in the period in which they occur.

Financial assets at fair value through profit or loss are recognised on trade date – the date on which the Bank commits to purchase the asset. Financial assets are derecognised when the rights to receive cash flows have expired or have been transferred and the Bank has transferred substantially all risks and rewards of ownership.

A strategic equity investment held by Treasury (see Note 23) was designated at transition to be measured at fair value through other comprehensive income. This election was made on an individual investment basis and is irrevocable. At initial recognition, this asset was measured at fair value. All fair value gains or losses are recognised in the statement of comprehensive income and not recycled through the income statement. Dividend income is recognised in the income statement in accordance with IAS 18 Revenue, unless this is a return on investment.

Financial liabilities

Financial liabilities at fair value through profit or loss

This category has two sub-categories: financial liabilities held for trading, and those designated at fair value through profit or loss upon initial recognition.

Derivative liabilities, except those forming part of a designated and effective hedging relationship, are also categorised as held for trading.

Other financial liabilities

With the exception of liabilities designated at fair value through profit or loss, all other financial liabilities are measured at amortised cost, unless they form part of a qualifying hedge relationship with a derivative position.

Derivative financial instruments and hedge accounting

All derivatives are measured at fair value through the income statement unless they form part of a qualifying cash flow hedging relationship. In this case, the fair value of the derivative is taken to reserves to the extent that it is a qualifying hedge of the identified risk. Any hedge ineffectiveness will result in the relevant proportion of the fair value remaining in the income statement. Fair values are derived primarily from discounted cash-flow models, option-pricing models and from third-party quotes. Derivatives are carried as assets when their fair value is positive, and as liabilities when their fair value is negative. All hedging activity is explicitly identified and documented by the Bank's Treasury department.

Hedge accounting

Hedge accounting is designed to bring accounting consistency to financial instruments that would not otherwise be permitted. A valid hedge relationship exists when a specific relationship can be identified between two or more financial instruments in which the change in value of one instrument (the hedging instrument) is highly negatively correlated to the change in value of the other (the hedged item). To qualify for hedge accounting this correlation must be within a range of 80 to 125 per cent, with any ineffectiveness within these boundaries recognised within "Fair value movement on non-qualifying and ineffective hedges" in the income statement. The Bank applies hedge accounting treatment to individually identified hedge relationships. Also included within this caption of the income statement are the gains and losses attributable to derivatives that the Bank uses for hedging interest-rate risk on a macro basis, but for which the Bank does not apply hedge accounting.

The Bank documents the relationship between hedging instruments and hedged items upon initial recognition of the transaction. The Bank also documents its assessment, on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

Fair value hedges

The Bank's hedging activities are primarily designed to mitigate interest rate risk by using swaps to convert the interest rate risk profile, on both assets and liabilities, into floating rate risk. Such hedges are known as "fair value" hedges. Changes in the fair value of the derivatives that are designated and qualify as fair value hedges, and that prove to be highly effective in relation to hedged risk, are included in the income statement, along with the corresponding change in fair value of the hedged asset or liability that is attributable to that specific hedged risk.

Cash flow hedges

The Bank has engaged in cash flow hedges, principally to minimise the exchange rate risk associated with the fact that its future administrative expenses are incurred in sterling. The amount and timing of such hedges fluctuates in line with the Bank's view on opportune moments to execute the hedges. Hedging is mainly through the purchase of sterling in the forward foreign exchange market, but currency options can also be used. The movement in the fair value of cash flow hedges is recognised directly in reserves until such time as the relevant expenditure is incurred. At 31 December 2010 the Bank had a number of cash flow hedges in place for future budgeted administrative expenditure to be incurred in sterling.

For further information on risk and related management policies see the "Risk management" section on page 28.

Financial guarantees

Issued financial guarantees are initially recognised at their fair value, and subsequently measured at the higher of the unamortised balance of the related fees received and deferred, and the expenditure required to settle the commitment at the statement of financial position date. The latter is recognised when it is both probable that the guarantee will need to be settled and that the settlement amount can be reliably estimated. Financial guarantees are recognised within other financial assets and other financial liabilities.

Impairment of financial assets

Financial assets at amortised cost

Where there is objective evidence that an identified loan asset is impaired, specific provisions for impairment are recognised in the income statement. Impairment is quantified as the difference between the carrying amount of the asset and the net present value of expected future cash flows discounted at the asset's original effective interest rate where applicable. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. The carrying amount of the asset is reduced directly only upon write-off. Resulting adjustments include the unwinding of the discount in the income statement over the life of the asset, and any adjustments required in respect of a reassessment of the initial impairment.

The criteria that the Bank uses to determine that there is objective evidence of an impairment loss include:

- delinquency in contractual payments of principal or interest
- cash flow difficulties experienced by the borrower
- breach of loan covenants or conditions
- initiation of bankruptcy proceedings
- deterioration in the borrower's competitive position
- deterioration in the value of collateral.

Provisions for impairment of classes of similar assets that are not individually identified as impaired are calculated on a portfolio basis. The methodology used for assessing such impairment is based on a risk-rated approach for non-sovereign assets. A separate methodology is applied for all sovereign risk assets that takes into account the Bank's preferred creditor status afforded by its members. The Bank's methodology calculates impairment on an incurred loss basis. Impairment is deducted from the asset categories on the statement of financial position.

The Bank maintains a loan loss reserve to set aside an amount of retained earnings within members' equity equal to the difference between the impairment losses expected over the full life of the loan portfolio, and the cumulative amount provisioned through the Bank's income statement on an incurred loss basis.

Impairment, less any amounts reversed during the year, is charged to the income statement. When a loan is deemed uncollectible the principal is written off against the related impairment provision. Such loans are written off only after all necessary procedures have been completed and the amount of the loss has been determined. Recoveries are credited to the income statement if previously written off.

Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months maturity from the date of the statement of financial position, which are available for use at short notice and that are subject to insignificant risk of changes in value.

Foreign currencies

The Bank's reporting currency for the presentation of its financial statements is the euro (€).

Foreign currency transactions are initially translated into euro using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions, and from the translation at the year-end exchange rate of monetary assets and liabilities denominated in foreign currencies, are included in the income statement, except when deferred in reserves as qualifying cash flow hedges.

Capital subscriptions

The Bank's share capital is denominated in euro.

Intangible assets

Costs associated with maintaining computer software programmes are recognised as an expense as incurred. Costs that are directly associated with identifiable and unique software products controlled by the Bank, and that will generate economic benefits exceeding costs beyond one year, are recognised as intangible assets. Direct costs include the staff costs of the software development team and an appropriate portion of relevant overheads.

Expenditure that enhances or extends the performance of computer software programmes beyond their original specifications is recognised as a capital improvement and is added to the original cost of the software. Computer software development costs recognised as intangible assets are amortised using the straight-line method over an estimated life of three years.

Property, technology and office equipment

Property, technology and office equipment is stated at cost less accumulated depreciation. Depreciation is calculated on the straight-line method to write off the cost of each asset to its residual value over the estimated life as follows:

Freehold property	30 years
Improvements on leases of less than 50 years unexpired	Unexpired periods
Technology and office equipment	Three years

Accounting for leases

Leases of assets under which all the risks and benefits of ownership are effectively retained by the lessor are classified as operating leases. The Bank has entered into such leases for most of its office accommodation, both in London and in the Bank's countries of operations. Payments made under operating leases are charged to the income statement on a straight-line basis over the period of the lease. When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which the termination takes place.

Interest, fees, commissions and dividends

Interest is recorded on an accruals basis using the effective interest method. Interest is recognised on impaired loans through unwinding the discount used in the present value calculations applied to expected future cash flows. Interest accrued for loans at fair value through profit or loss is recognised in the interest line of the income statement.

Front-end fees and commitment fees are deferred in accordance with IAS 18, together with the related direct costs of originating and maintaining the commitment. These are then recognised in interest income using the effective interest method over the period from disbursement to repayment of the related loan. If the commitment expires without the loan being drawn down, the fee is recognised as income on expiry.

Fees received in respect of services provided over a period of time are recognised as income as the services are provided. Other fees and commissions are classed as income when received. Issuance fees and redemption premiums or discounts are amortised over the period to maturity of the related borrowings on an effective yield basis.

Dividends relating to share investments are recognised in accordance with IAS 18 Revenue.

Staff retirement plans

The Bank has a defined contribution scheme and a defined benefit scheme to provide retirement benefits to its staff. Under the defined contribution scheme, the Bank and staff contribute to provide a lump sum benefit. The defined benefit scheme is funded entirely by the Bank and benefits are based on years of service and a percentage of final gross base salary as defined in the scheme.

The asset in respect of the defined benefit scheme is the fair value of plan assets minus the present value of the defined benefit obligation at the statement of financial position date, together with adjustments for unrecognised actuarial gains/losses and past service cost. Independent actuaries calculate the defined benefit obligation at least every three years by using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows (relating to service accrued to the statement of financial position date) using the yields available on high-quality corporate bonds. For intermediate years, the defined benefit obligation is estimated using approximate actuarial roll-forward techniques that allow for additional benefit accrual, actual cash flows and changes in the underlying actuarial assumptions.

The Bank keeps all contributions to the schemes, and all other assets and income held for the purposes of the schemes, separately from all of its other assets. Actual contributions made to the defined contribution scheme are charged to the income statement and transferred to the scheme's independent custodians. The charge to the income statement in respect of the defined benefit scheme is based on the current service cost and other actuarial adjustments, as determined by qualified external actuaries. Also included in this charge are actuarial gains and losses in excess of a 10 per cent corridor that are amortised over the estimated average service life remaining of the Bank's employees. The 10 per cent corridor is the higher of 10 per cent of the defined benefit obligation or the fair value of assets. The Bank's contributions to the defined benefit scheme are determined by the Retirement Plan Committee, with advice from the Bank's actuaries, and the contributions are transferred to the scheme's independent custodians.

Taxation

In accordance with Article 53 of the Agreement, within the scope of its official activities, the Bank, its assets, property and income are exempt from all direct taxes and all taxes and duties levied upon goods and services acquired or imported, except for those parts of taxes or duties that represent charges for public utility services.

Borrowings

Borrowings are recognised initially at fair value, defined as their issue proceeds, net of any transaction costs incurred. They are subsequently stated at amortised cost and any difference between net proceeds and the redemption value is recognised in the income statement over the period of the borrowings using the effective yield method. Where borrowings have associated derivatives and qualify for fair value hedge accounting in line with IAS 39, the amortised cost value is adjusted by the fair value of the hedged risks.

Comparatives

The Bank opted to apply IFRS 9 from 1 January 2010, as well as the related amendments to other IFRSs, because the new accounting standard better reflects the Bank's business model for managing such assets. In accordance with the transition provisions of the standard, comparative figures have not been restated.

Financial assets – classification prior to 1 January 2010

The Bank classifies its financial assets in the following categories: loans and receivables; financial assets at fair value through profit or loss; available-for-sale financial assets; and held-to-maturity investments. Management determines the classification of its investments upon initial recognition with the exception of those reclassified under the amendment to IAS 39.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market upon initial recognition or reclassification, other than:

- those that the Bank intends to sell immediately or in the short term, which are classified as held for trading, and those that the Bank designates at fair value through profit or loss upon initial recognition
- those that the Bank designates as available-for-sale upon initial recognition
- those for which the Bank may not recover substantially all of its initial investment, other than because of credit deterioration.

Loans and receivables originated by the Bank are recognised at settlement date and measured at amortised cost using the effective interest method less any provision for impairment or un-collectability, unless they form part of a qualifying hedging relationship with a derivative position. This principally occurs in cases of fixed rate loans that, through association with individual swaps, are transformed from a fixed rate basis to a floating rate basis. In such cases, the loan is re-measured to fair value in respect of interest rate risk. The change in value is then reported in the income statement as an offset to the change in value of the related swap if the hedge relationship is highly effective – see “Derivative financial instruments and hedge accounting” on page 20 for details. Pursuant to the amendment to IAS 39, if an instrument previously classified as available-for-sale subsequently satisfies the definition of loans and receivables, then it may be reclassified. Once reclassified, the loan is held at amortised cost and interest is recognised using the effective interest rate on the date of reclassification. The Bank opted to reclassify a substantial portion of its available-for-sale debt securities portfolio into the category loans and receivables effective 1 July 2008, on the basis that the market for those securities had become inactive and the Bank has the intention and ability to hold the securities for the foreseeable future.

Collateralised placements are carried at amortised cost. These are structures wherein the risks and rewards associated with the ownership of a reference asset are transferred to another party through the use of a “total return” swap contract, and are a form of collateralised lending.

Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss upon initial recognition.

A financial asset is classified as held for trading if it is:

- acquired or incurred principally for the purpose of selling or repurchasing in the near term
- part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking
- a derivative, except those forming part of a designated and effective hedging relationship.

The Bank classifies assets acquired for the purpose of generating profits from short-term price fluctuations as held for trading. Such assets are accounted for at fair value on the basis of independent market quotations, with all changes in value recorded through the income statement as they occur.

Financial assets are designated at fair value through profit or loss upon initial recognition when:

- doing so significantly reduces measurement inconsistencies that would arise if the related derivatives were treated as held for trading and the underlying financial instruments were carried at amortised cost
- certain investments, such as share investments, that are managed and evaluated on a fair value basis in accordance with a documented risk management or investment strategy and reported to key management personnel on that basis are designated at fair value through profit and loss
- financial instruments, such as debt securities, containing one or more embedded derivatives that significantly modify the cash flows, are designated at fair value through profit and loss.

The Bank designates associate share investments and high-risk equity funds at fair value through profit or loss upon initial recognition using the IAS 28 “venture capital” exemption, as the Bank considers these to be venture capital investments. Such assets are carried at fair value on the statement of financial position with changes in fair value included in the income statement in the period in which they occur. The basis of fair value for listed associate share investments and high risk equity funds in an active market is the quoted bid market price on the statement of financial position date. The basis of fair value for associate share investments and high risk equity funds that are either unlisted or listed in an inactive market is determined using valuation techniques appropriate to the market and industry of each investment. The primary valuation techniques used are net asset value and earnings-based valuations using comparable information and discounted cash flows. Techniques used to support these valuations include industry valuation benchmarks and recent transaction prices.

All debt securities held in externally managed funds have been designated at fair value through profit or loss upon initial recognition as they are managed and evaluated on a fair value basis in accordance with the documented investment strategy.

Financial assets measured at fair value through profit or loss are recognised or derecognised at trade date – the date on which the Bank commits to purchase or sell the asset.

Available-for-sale

Available-for-sale investments are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices. Purchases and sales of available-for-sale assets are recognised at trade date.

With the exception of those share investments designated at fair value through profit or loss, the Bank classifies all other share investments as available-for-sale. Such assets are carried at fair value on the statement of financial position. Changes in fair value, including translation differences arising on assets denominated in foreign currencies, are recognised directly in reserves until the financial asset is sold or impaired. At this time the cumulative gain or loss previously recognised in reserves is removed and included in the income statement. The basis of fair value for available-for-sale share investments listed in an active market is the quoted bid market price on the statement of financial position date. The basis of fair value for available-for-sale share investments that are unlisted or listed in an inactive market is determined using valuation techniques appropriate to the market and industry of each investment. The primary valuation techniques used are net asset value and earnings-based valuations using comparable information and discounted cash flows. Techniques used to support these valuations include industry valuation benchmarks and recent transaction prices.

A portion of the Treasury debt securities portfolio is classified as available-for-sale. Such assets are carried at fair value on the statement of financial position with fair values determined by bid quotes from third-party sources. Changes in fair value, excluding translation differences arising on assets denominated in foreign currencies, are recognised directly in reserves until the financial asset is sold or impaired. At this time the cumulative gain or loss previously recognised in reserves is removed and included in the income statement. Foreign currency translation differences arising on Treasury available-for-sale debt assets are recognised in the income statement.

Where an available-for-sale asset is the hedged item in a qualifying fair value hedge, the fair value gain or loss attributable to the risk being hedged is reported in the income statement rather than reserves. This is to ensure there is consistency of reporting, as the fair value changes on the derivative acting as the hedge must be reported in the income statement. Hedge accounting features in Treasury positions where asset swaps are used to transform the returns on fixed interest rate securities to a floating rate basis.

Held-to-maturity

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Bank has the intention and ability to hold to maturity. The Bank classifies short-dated instruments such as commercial paper and government-issued bills in this category.

Impairment of available-for-sale share investments (applicable to 31 December 2009)

Available-for-sale share investments are impaired when there is objective evidence that the future recoverability of the Bank's original investment is in doubt. A significant or prolonged decline in the fair value of a share investment below its cost represents objective evidence of impairment. The Bank also evaluates factors such as country, industry and sector performance, changes in technology and operational and financial performance. Although projects are usually reviewed for impairment every six months, or, in the case of low risk projects, at least once a year, certain events may trigger this process sooner and more frequently. In such cases, future collectability is considered and any cumulative loss previously recognised in reserves is removed and included in the income statement.

Impairment losses recognised in operating income for available-for-sale share investments are not reversed through the income statement.

Impairment of available-for-sale debt securities (applicable to 31 December 2009)

The Bank assesses at each statement of financial position date whether there is objective evidence of impairment. The criteria that the Bank uses to determine that there is objective evidence of an impairment loss include:

- downgrading of the issuer below minimum eligibility levels for Treasury exposures
- issuer failure to pay amounts contracted under the security
- covenant breaches, default events and trigger level failures
- deterioration of credit enhancement including diminution of collateral values
- legal proceedings such as bankruptcy, regulatory action or similar.

If any such evidence exists, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in operating income – is removed from reserves and recognised in the income statement. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases, and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, the impairment loss is reversed through the income statement.

C. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Preparing financial statements in conformity with IFRS requires the Bank to make estimates and judgements that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts included in the income statement during the reporting period. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

These estimates are highly dependent on a number of variables that reflect the economic environment and financial markets of the Bank's countries of operations, but which are not directly correlated to market risks such as interest rate and foreign exchange risk. The Bank's critical accounting estimates and judgements are as follows.

Fair value of derivative financial instruments

The fair values of the Bank's derivative financial instruments are determined by using discounted cash flow models. These cash flow models are based on underlying market prices for currencies, interest rates and option volatilities. Where market data is not available for all elements of a derivative's valuation, extrapolation and interpolation of existing data has been used. Where unobservable market data has been used, a sensitivity analysis has been included under "Fair value hierarchy" on page 57.

Fair value of Banking loans at fair value through profit or loss

The fair values of the Bank's loans at fair value through profit or loss are determined by using a combination of discounted cash flow models and options pricing models. These models incorporate market data pertaining to interest rates, borrower's credit spreads, underlying equity prices and dividend cash flows. Where relevant market data is not available extrapolation and interpolation of existing data has been used. Where unobservable market data has been used, a sensitivity analysis has been included under "Fair value hierarchy" on page 57.

Fair value of share investments

The Bank's method for determining the fair value of share investments is described in the "Financial assets" accounting policy on page 19 and an analysis of the share investment portfolio is provided in Note 22. In relation to the Bank's share investments where the valuations are not based on observable market inputs, additional sensitivity information has been included under "Fair value hierarchy" on page 57.

Impairment of available-for-sale share investments (applicable to 31 December 2009)

Under IAS 39, the key indicator of equity impairment is a “significant or prolonged decline in the fair value of an investment in an instrument below cost”. For the Bank, a “significant” decline is defined as a decline greater than 30 per cent below cost. This figure reflects the assessment that, in the current financial markets, any decline less than 30 per cent may not be an indicator of permanent impairment. A “prolonged” decline is defined as a decline below cost for greater than 12 months.

As a measure of sensitivity for “significant” decline:

- If an impairment trigger of a decline greater than 20 per cent below cost was applied with the “prolonged” decline trigger held constant, a further six available-for-sale share investments with a fair value totalling €12 million at 31 December 2009 would potentially be classified as impaired.
- If an impairment trigger of a decline greater than 40 per cent below cost was applied with the “prolonged” decline trigger held constant, one available-for-sale share investment with a fair value totalling €3 million at 31 December 2009 would potentially not be classified as impaired.

As a measure of sensitivity for “prolonged” decline:

- If an impairment trigger of a decline below cost for greater than six months was applied with the “significant” decline trigger held constant, a further five available-for-sale share investments with a fair value totalling €20 million at 31 December 2009 would potentially be classified as impaired.
- If an impairment trigger of a decline below cost for greater than 18 months was applied with the “significant” decline trigger held constant, this would not result in any additional impairments.

Provisions for the impairment of loan investments

The Bank’s method for determining the level of impairment of loan investments is described in the “Impairment of financial assets” accounting policy on page 21 and further explained under “Credit risk” on page 28.

Portfolio provisions for the unidentified impairment of non-sovereign loan investments at 31 December 2010 were €378 million. The sensitivity of portfolio provisions to uniform risk rating upgrades, downgrades, and a change in loss given default assumptions is provided below.

Risk ratings

- If all non-sovereign loan investments were upgraded by one category on the Bank’s probability of default rating, this would result in a credit to the income statement of €356 million. This credit is due to a reduction of €204 million in portfolio provisions on loan investments, and a reduction of €152 million in specific provisions.
- Conversely, if all non-sovereign loan investments were downgraded by one category on the Bank’s probability of default rating this would result in a total charge to the income statement of €1.1 billion. This comprises a charge to the income statement of €137 million in relation to portfolio provisions for non-sovereign loans. On downgrade by one probability of default rating category, 13 per cent of non-sovereign loan investments would become individually impaired. Consequently, specific provisions for identified impairment would have increased by approximately €1.0 billion.

Probability of default rates

- In determining the probabilities of default for each risk rating, the relative weighting applied to external data and Bank’s own experience is reviewed annually. The 2010 general provisioning methodology applies a 50 per cent weighting to the Bank’s own experience and a 50 per cent weighting to external data. This constitutes a change from the previous year’s methodology whereby a 25 per cent weighting was applied to the Bank’s own experience (75 per cent external default data), reflecting an increase in the availability and relevance of internal data. Had the 25 per cent weighting of the Bank’s default experience remained effective in 2010, the portfolio provisions for the unidentified impairment of non-sovereign loan investments would have been €110 million higher at €488 million. If the weighting of the Bank’s default experience was increased from 50 per cent to 75 per cent, the portfolio provision for the unidentified impairment of non-sovereign loan investments would have been €110 million lower at €268 million.

Loss given default rates

- A decrease in loss given default rates by 10 percentage points would lead to a decrease in portfolio provisions of €59 million, reducing provisions for unidentified impairment in non-sovereign loans to €319 million.
- An increase in loss given default rates by 10 percentage points would lead to an increase in portfolio provisions for unidentified impairment of non-sovereign loans by €58 million, to a total of €436 million.

Sovereign ratings

- Portfolio provisions for the unidentified impairment of sovereign loan investments at 31 December 2010 amounted to €12 million (2009: €12 million). Due to the Bank's preferred creditor status afforded by its members, a downgrade or upgrade by one risk rating category would not have had a significant impact on the level of sovereign portfolio provisions, and hence the income statement.

The methodology and judgements used for estimating provisions for the impairment of loan investments are reviewed annually to reduce any differences between loss estimates and actual experience.

Risk management

FINANCIAL RISKS

The independent identification, measurement, monitoring and mitigation of all risks incurred by the Bank in both its Banking and Treasury activities is the overall responsibility of the Vice President, Risk and Resources.

The Vice President, Risk and Resources is a member of the Bank's Executive Committee, as are the First Vice President, Banking, and the Vice President, Finance and Chief Financial Officer to whom Treasury reports. The Vice President, Risk and Resources, has overall responsibility for formulating the Bank's risk management strategy for both Banking and Treasury functions. Risk Management seeks to ensure that any risks are correctly identified and appropriately managed and mitigated through comprehensive and rigorous processes, which reflect industry best practice.

In carrying out its mission, the Bank is exposed to financial risks through both its Banking and Treasury activities. The principal financial risks to which the Bank is exposed are credit, market and liquidity risk. The last year saw a rebound in equity markets and the possible beginning of a transition from systemic to differentiated risk. While risk, as measured by the Bank, has continued to increase from last year, no significant realisations of those increased risks have occurred through defaults.

A. CREDIT RISK

Credit risk is the potential loss to a portfolio that could result from the default of a counterparty or the deterioration of its creditworthiness. The Bank also monitors concentration risk, which is the risk arising from too high a proportion of the portfolio being allocated to a specific country, industry sector, obligor, and type of instrument or individual transaction.

The Bank is exposed to credit risk in both its Banking and Treasury activities, as borrowers and Treasury counterparties could default on their contractual obligations, or the value of the Bank's investments could become impaired.

Maximum exposure to credit risk before collateral held or other credit enhancements

	2010 € million	2009 € million
Placements with and advances to credit institutions	2,974	3,247
Debt securities at fair value through profit or loss	737	222
Debt securities at amortised cost	8,955	–
Collateralised placements	1,179	1,171
Available-for-sale debt securities	–	1,012
Held-to-maturity debt securities	–	1,239
Derivative financial assets	4,168	2,538
Other financial assets	525	483
Treasury loan investments	–	5,321
Banking loan investments at amortised cost	14,613	12,406
Banking loan investments at fair value	221	–
Paid-in capital receivable	16	17
Undrawn commitments and guarantees	9,394	7,716
At 31 December	42,782	35,372

The above table represents the worst-case scenario of credit risk exposure to the Bank at 31 December 2010 and 31 December 2009, without taking account of any collateral held or other credit enhancements.

Credit risk in the Banking portfolio: Management

For Banking exposures the Board of Directors approves a credit process document that defines the procedures for the approval, management and review of Banking exposures by the Operations Committee. The Audit Committee reviews the credit process annually and its review is submitted to the Board for approval.

Banking projects are reviewed by the Operations Committee. The Operations Committee is chaired by the First Vice President, Banking and its membership comprises senior managers of the Bank. The Operations Committee is responsible for reviewing all Banking operations prior to their submission for Board approval. Projects are reviewed to ensure they meet the Bank's criteria for sound banking, transition impact and additionality. The Operations Committee operates within the authority delegated by the

Board, via the Executive Committee, to approve projects within Board-approved framework operations. The Operations Committee is also responsible for overseeing Banking portfolio management, approving significant changes to existing operations and approving Risk Management's recommendations for provisions for the impairment of Banking loans.

The Bank conducts regular reviews of all exposures within the Banking portfolio, typically on a semi-annual basis. Exposures that are perceived to be more vulnerable to possible default are reviewed more frequently and those that are perceived to be less vulnerable may be reviewed annually. At each review, Risk Management assesses whether there has been any change in the risk profile of the exposure, recommends actions to mitigate risk and reconfirms or adjusts the risk rating. For share investments it also reviews the fair value. At the recommendation of Risk Management, investments considered to be in jeopardy may be transferred from Banking teams to the Corporate Recovery Unit – which reports jointly to Risk Management and Banking – in order to manage the restructuring work-out and recovery process.

The table below shows the Bank's internal rating scale and how this approximately maps to the external ratings of Standard & Poor's (S&P).

EBRD internal rating scale	External rating equivalent – S&P	EBRD category
1	AAA	Excellent
2	AA+, AA, AA-	Strong
3	A+, A, A-	Very good
4	BBB+, BBB, BBB-	Good
5	BB+, BB, BB-	Satisfactory
6	B+, B	Acceptable
6W	B-	Watch
7	CCC	Special attention
8	CC	Substandard
9	C	Doubtful
10	D	Expected loss

As a response to the financial crisis, resources in the Banking division are being applied to sectors at more immediate risk (for example, financial institutions), and monitoring has been intensified to ensure a timely response to potential credit problems.

Disbursements are managed by the Operations Administration Unit (OAU) within the Office of the General Counsel. The OAU is responsible for checking compliance with the loan agreements and other project agreements and ensuring that correct procedures are followed in line with approved policy. Waivers, consents and amendments of loan covenants and conditionality are prepared by the OAU and are approved by Banking, Risk Management and, where required, by the Office of the General Counsel, the Office of the Chief Economist and the Environment and Sustainability Department.

The portfolio provisioning methodology was revised during the year to better reflect the actual loss experience of the Bank. The general portfolio provisions are assessed on a granular basis based on assumption values assigned to probabilities of default and loss given default parameters for each exposure, including separate assessment of exposures guaranteed by third parties. The general portfolio provisions are therefore computed under a more granular methodology than in previous years. The combined or aggregated impact of these parameters forms the basis for the Bank's facility risk ratings. In line with current reporting to management and consistent with previous years, this risk note discloses these aggregated facility risk ratings.

Risk Management prepares a report on the development of the portfolio as a whole on a quarterly basis to present to the Audit Committee. The report includes a summary of key factors affecting the portfolio and provides analysis and commentary on trends within the portfolio. It also includes commentary on individual exposures in the classified portfolio and measures of exposure against portfolio risk limits, with any breaches of limits reported and explained.

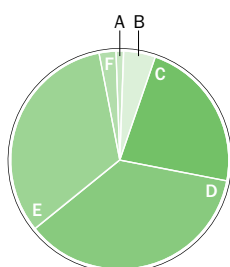
The Bank assigns project, country and overall risk ratings to each exposure on an internal scale from 1 (lowest risk) to 10 (highest risk). The project rating is determined on the basis of the financial strength of the risk counterparty and the risk mitigation built into the project structure, including sponsor support or guarantee. The country rating is assessed internally, taking into consideration the ratings assessed by external rating agencies. For non-sovereign operations, the overall rating is normally the numerically higher of the project and country rating. The exception to this is where the Bank has recourse to unconditional sponsor support from outside the country of operations, in which case the overall rating is the same as the project rating. For sovereign risk projects, the overall rating is the same as the country rating.

Credit risk in the Banking portfolio: 2010 results

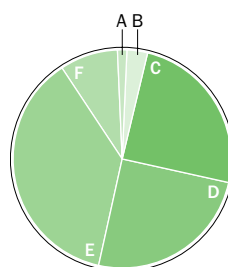
The total Banking exposure (operating assets including fair value adjustments but before provisions) increased during the year from €17.9 billion at 31 December 2009 to €21.3 billion at 31 December 2010. The total signed Banking portfolio (operating assets, excluding fair value adjustments and provisions but including undrawn commitments) increased from €25.6 billion at 31 December 2009 to €30.6 billion at 31 December 2010. The overall risk rating of the portfolio improved slightly from 6.12 to 5.94.

Total non-sovereign operating assets risk rated 7 to 10 decreased, both in real terms and as a proportion of the portfolio, from €5.2 billion (29 per cent of total operating assets) to €4.1 billion (19 per cent of total operating assets). Impaired loan assets increased from €305 million to €465 million due to the continued economic downturn, ongoing liquidity and corporate troubles in many of the Bank's countries of operations.

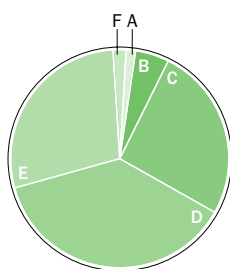
Upon adoption of IFRS 9, impairment is no longer required for the Bank's share investments. This means there will no longer be impairment triggers resulting in a downgrade of the investment's risk rating as fair value is the only measurement basis. As such, there was a €1.3 billion decrease in share investments risk-rated 8 to 10, from €1.6 billion at 31 December 2009 to €256 million at 31 December 2010.

Credit quality of the Banking portfolio**31 December 2010**

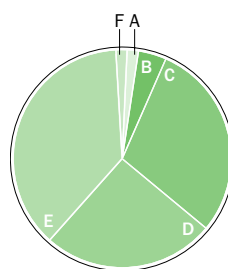
A	1, 2, 3	1.3%
B	4	4.8%
C	5	22.6%
D	6	36.3%
E	6W, 7	32.6%
F	8, 9, 10	2.4%

**31 December 2009**

A	1, 2, 3	1.4%
B	4	3.3%
C	5	24.5%
D	6	25.0%
E	6W, 7	37.3%
F	8, 9, 10	8.5%

Credit quality of the loan portfolio**31 December 2010¹⁵**

A	1, 2, 3	1.5%
B	4	5.1%
C	5	25.6%
D	6	37.7%
E	6W, 7	28.1%
F	8, 9, 10	2.0%

**31 December 2009**

A	1, 2, 3	1.9%
B	4	4.0%
C	5	29.5%
D	6	25.7%
E	6W, 7	37.3%
F	8, 9, 10	1.6%

¹⁵ From an accounting perspective, there is no credit risk exposure on Banking share investments as they are fair valued and "fair value" is defined as "the amount for which an asset ... could be exchanged, between knowledgeable, willing parties in an arm's length transaction" (IFRS 9: Appendix A).

Loan investments at amortised cost

Set out below is an analysis of the Banking loan investments and the associated impairment provisions for each of the Bank's internal risk rating categories.

Risk rating	Neither past due nor impaired € million	Past due but not impaired € million	Impaired € million	Total € million	Total %	Portfolio provisions for unidentified impairment € million	Specific provisions for identified impairment € million	Total net of impairment € million	Impairment provisions %
2: Strong	25	-	-	25	0.2	-	-	25	0.0
3: Very good	133	-	-	133	0.9	(1)	-	132	0.8
4: Good	949	-	-	949	6.2	(11)	-	938	1.2
5: Satisfactory	4,560	-	-	4,560	29.9	(38)	-	4,522	0.8
6: Acceptable	5,249	-	-	5,249	34.4	(86)	-	5,163	1.6
6W: Watch	1,856	-	-	1,856	12.2	(75)	-	1,781	4.0
7: Special attention	1,987	19	-	2,006	13.1	(179)	-	1,827	8.9
8: Substandard	-	-	375	375	2.5	-	(152)	223	40.5
9: Doubtful	-	-	18	18	0.1	-	(16)	2	88.9
10: Expected loss	-	-	72	72	0.5	-	(72)	-	100.0
At 31 December 2010	14,759	19	465	15,243	100.0	(390)	(240)	14,613	-

Risk rating	Neither past due nor impaired € million	Past due but not impaired € million	Impaired € million	Total € million	Total %	Portfolio provisions for unidentified impairment € million	Specific provisions for identified impairment € million	Total net of impairment € million	Impairment provisions %
2: Strong	45	-	-	45	0.3	-	-	45	0.0
3: Very good	254	-	-	254	1.9	-	-	254	0.0
4: Good	744	-	-	744	5.7	(1)	-	743	0.1
5: Satisfactory	4,295	4	-	4,299	32.8	(22)	-	4,277	0.5
6: Acceptable	2,816	-	-	2,816	21.5	(45)	-	2,771	1.6
6W: Watch	1,646	1	-	1,647	12.5	(72)	-	1,575	4.4
7: Special attention	2,991	24	-	3,015	23.0	(363)	-	2,652	12.0
8: Substandard	-	-	163	163	1.2	-	(76)	87	46.6
9: Doubtful	-	-	6	6	0.1	-	(4)	2	66.7
10: Expected loss	-	-	136	136	1.0	-	(136)	-	100.0
At 31 December 2009	12,791	29	305	13,125	100.0	(503)	(216)	12,406	-

There were 11 renegotiated loans (2009: 12) during the year that would otherwise have been past due or impaired. At 31 December 2010 these loans totalled €26 million (2009: €99 million).

Of the past due loans, none were outstanding for less than 30 days (2009: €6 million), €12 million were outstanding for more than 30 days but less than 90 days (2009: €13 million) and €7 million were outstanding for more than 90 days (2009: €16 million).

The fair value of collateral held over impaired and past due loans at 31 December 2010 was €224 million (2009: €99 million).

Loans at fair value through profit or loss

Set out below is an analysis of the Bank's loans at fair value through profit or loss for each of the Bank's relevant internal risk rating categories. No comparatives are required upon early adoption of IFRS 9.

Risk rating	Fair value 2010 € million
5: Satisfactory	15
6: Acceptable	12
6W: Watch	123
7: Special attention	71
At 31 December	221

Undrawn commitments and guarantees

Set out below is an analysis of the Bank's undrawn commitments and guarantees for each of the Bank's relevant internal risk rating categories.

Risk rating	Undrawn commitments 2010 € million	Guarantees 2010 € million	Undrawn commitments 2009 € million	Guarantees 2009 € million
2: Strong	4	–	4	–
3: Very good	42	–	62	–
4: Good	378	–	20	–
5: Satisfactory	1,335	63	1,340	54
6: Acceptable	4,101	109	2,740	82
6W: Watch	1,674	153	1,486	112
7: Special attention	1,387	140	1,364	76
8: Substandard	6	–	368	–
9: Doubtful	2	–	7	1
At 31 December	8,929	465	7,391	325

For projects risk rated 8 or worse, it is unlikely that commitments would be drawn down given that conditions precedent need to be satisfied before further disbursements.

Paid-in capital receivable

Set out below is an analysis of the Bank's paid-in capital receivable at 31 December 2010 and 31 December 2009.

	2010 € million	2009 € million
Cash and promissory notes due but not yet received	16	17
Paid-in capital receivable at 31 December	16	17

At 31 December 2010 no paid-in capital receivable was considered impaired (2009: nil).

Credit risk in the Banking portfolio: Concentration

The following table breaks down the main Banking credit risk exposures in their carrying amounts by geographic region.

	Loans 2010 € million	Undrawn commitments and guarantees 2010 € million	Total 2010 € million	Loans 2009 € million	Undrawn commitments and guarantees 2009 € million	Total 2009 € million
Albania	211	132	343	177	134	311
Armenia	169	30	199	104	70	174
Azerbaijan	407	107	514	324	212	536
Belarus	83	31	114	75	27	102
Bosnia and Herzegovina	392	485	877	356	408	764
Bulgaria	728	398	1,126	599	202	801
Croatia	752	163	915	620	97	717
Czech Republic	43	4	47	54	7	61
Estonia	-	2	2	-	8	8
Former Yugoslav Republic of Macedonia	123	99	222	136	87	223
Georgia	304	306	610	248	74	322
Hungary	495	185	680	304	507	811
Kazakhstan	766	751	1,517	597	428	1,025
Kyrgyz Republic	39	36	75	31	44	75
Latvia	20	97	117	34	12	46
Lithuania	143	16	159	79	20	99
Moldova	135	116	251	84	90	174
Mongolia	162	14	176	46	16	62
Montenegro	60	146	206	52	28	80
Poland	832	319	1,151	691	166	857
Romania	1,510	576	2,086	1,263	601	1,864
Russia	4,173	1,461	5,634	3,997	1,377	5,374
Serbia	791	763	1,554	611	564	1,175
Slovak Republic	193	120	313	129	184	313
Slovenia	21	2	23	31	3	34
Tajikistan	39	29	68	36	23	59
Turkey	460	139	599	108	35	143
Turkmenistan	10	3	13	7	4	11
Ukraine	1,937	1,215	3,152	1,757	861	2,618
Uzbekistan	86	16	102	90	33	123
Regional	380	1,633	2,013	485	1,394	1,879
At 31 December	15,464	9,394	24,858	13,125	7,716	20,841

The following table breaks down the main Banking credit risk exposures in their carrying amounts by the industry sector of the counterparty.

	Loans 2010 € million	Undrawn commitments and guarantees 2010 € million	Total 2010 € million	Loans 2009 € million	Undrawn commitments and guarantees 2009 € million	Total 2009 € million
Agribusiness	1,507	465	1,972	1,339	333	1,672
Banking	4,064	1,206	5,270	3,024	1,172	4,196
Equity funds	–	828	828	–	728	728
Insurance and financial services	522	291	813	364	262	626
Manufacturing and services	1,867	622	2,489	1,851	371	2,222
Municipal and environmental infrastructure	1,063	1,049	2,112	1,039	824	1,863
Natural resources	1,283	374	1,657	726	354	1,080
Power and energy	1,708	1,350	3,058	1,281	1,033	2,314
Property and tourism	388	494	882	277	592	869
Small business finance	616	63	679	611	96	707
Telecoms, informatics and media	159	65	224	277	71	348
Transport	2,287	2,587	4,874	2,336	1,880	4,216
At 31 December	15,464	9,394	24,858	13,125	7,716	20,841

Credit risk in the Treasury portfolio: Management

For Treasury exposures, the Board of Directors approves a Treasury and Treasury Risk Management Authority (T&TRMA), which defines the risk parameters for funding, cash management, asset and liability management and the investment activities of the Bank. This document is updated annually by the Finance and Risk and Resources Vice Presidencies and approved by the Board. It covers all aspects of Treasury where financial risks arise and also Risk Management's identification, measurement, management and mitigation of the financial risks in Treasury. In addition, Treasury and Treasury Risk Management guidelines have been issued in respect of Treasury risk taking and the related risk management processes and procedures.

The T&TRMA is the document by which the Board of Directors delegates authority to the Vice President, Finance and Chief Financial Officer to manage and the Vice President, Risk and Resources, to identify, measure, monitor and mitigate the Bank's Treasury exposures. The two Vice Presidents jointly interpret the T&TRMA and notify the Board of Directors of any material interpretation. The Financial and Operations Policies Committee reviews the T&TRMA annually and its review is submitted to the Board for approval.

Treasury risks are reviewed by the Treasury Exposure Committee (TEC). The TEC is chaired by the Vice President, Finance and Chief Financial Officer and its membership comprises senior managers of the Bank. The TEC is responsible for reviewing and monitoring the implementation of the T&TRMA and related guidelines. It assesses Treasury and Risk Management policy proposals for approval by the Board, and monitors and reviews the asset/liability profile and risk/return trade off in aggregate Treasury exposures. It also evaluates new product proposals for Treasury. Impairment of Treasury assets is identified by Risk Management, assessed by the TEC and approved by the Vice Presidents of Finance and Risk and Resources.

Each counterparty or issuer to which the Bank is exposed through its Treasury activities is approved and granted a maximum credit limit by Risk Management. Risk Management assigns internal credit ratings based on internal analysis of approved counterparties' creditworthiness through the synthesis of externally provided credit research and market data, and with reference to external rating benchmarks from approved rating agencies. The internal credit rating scale ranges from 1 (lowest risk) to 10 (highest risk), the same as that used for Banking exposures (a table showing how the Bank's internal rating scale maps to the external ratings of S&P is shown in "Credit risk in the Banking portfolio: Management" on page 29).

Eligible Treasury exposures are normally rated between 1 and 3 (approximately equivalent to S&P AAA to A- ratings), with the exception of counterparties in the countries of operations approved for local currency activities. These transactions support the Bank's initiatives to provide local currency financing to Banking clients and to develop local capital markets. These internal ratings determine the maximum allowable exposures as set out per rating level and counterparty type in the Bank's guidelines for Treasury operations. The internal rating process is based on credit risk managers' judgement, external rating benchmarks and senior management oversight and approval. Risk Management assesses all available credit research to identify key counterparty credit risk considerations. That analysis is then supplemented with market-based credit indicators, such as credit default swap spreads and market-implied credit ratings, to produce an internal rating for each approved counterparty.

The assigned internal ratings are relative rankings of default risk. When analysing portfolio credit risk within Treasury activities, the Bank maps internal ratings to external rating benchmarks to apply rating transition and default statistics sourced from rating agencies.

The Board-approved T&TRMA states the minimum rating and maximum tenor by type of eligible counterparty. Operational guidelines approved and issued by the Vice President, Risk and Resources set the maximum exposure size limits per rating class and counterparty type. The actual exposure size limit and/or tenor limit attributed to individual counterparties may be smaller or shorter, respectively, based on the likely direction of its credit quality over the medium term, its internal outlook, or on sector considerations. Individual counterparty lines for banks, corporates and insurance companies are measured, monitored and reviewed by Risk Management on a regular basis with a strong surveillance focus, including quarterly reports on the counterparties either contributing the most to the credit Value at Risk (VaR) of the Treasury portfolio or with large nominal exposures.

The Bank's exposure measurement methodology for Treasury credit risk uses a "Monte Carlo" simulation technique that produces, to a high degree of confidence, maximum exposure amounts at future points in time for each counterparty (in practice, 95 per cent eVaR).¹⁶ This includes all transaction types and is measured out to the maturity of the longest dated transaction with that counterparty. Exposures are calculated and controlled against approved limits daily with exceptions escalated to the Director, Risk Management for approval. In 2010 there was a net release of impairments for the Treasury credit portfolio of €9 million (2009: charge of €32 million).

Risk mitigation techniques and risk transferring instruments reduce calculated credit exposure measures. For example, Credit Support Annexes for over-the-counter (OTC) derivatives activity reduce potential future exposures in line with collateral posting expectations. Likewise, buying credit protection via a credit default swap usually decreases measured exposure on the reference entity.

Credit risk in the Treasury portfolio: 2010 results

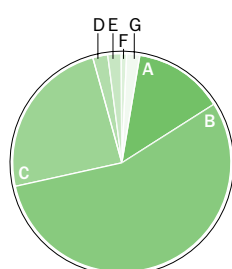
Treasury peak credit exposure stood at €11.2 billion at 31 December 2010 compared with €9.6 billion at 31 December 2009.

The credit quality of the Treasury portfolio slightly improved during 2010 with the average credit rating weighted by peak counterparty exposure standing at 2.43 at 31 December 2010 (2009: 2.45).¹⁷

The percentage of Treasury transactions of investment grade quality¹⁸ increased to 95 per cent at 31 December 2010 (2009: 93 per cent). Treasury's exposure to below investment grade obligors is limited to counterparties from the countries of operations, a few asset-backed security (ABS) investments originally rated triple-A by leading external rating agencies as well as the impaired financial sector bonds.

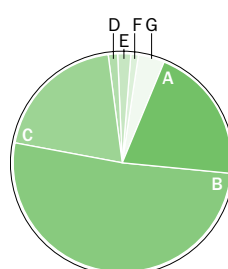
At 31 December 2010 there were no collateralised placements, Treasury share investments or other financial assets past due or impaired (2009: nil). All trades within these categories were risk rated 1 (excellent) to 3 (very good) on the Bank's internal risk rating scale (refer to page 29 for the Bank's full internal risk rating scale) for both 2010 and 2009. In 2009 there were no held-to-maturity debt securities past due or impaired and all trades were risk rated 1 to 3.

Credit quality of the Treasury portfolio



31 December 2010

A	1	13.6%
B	1.7–2.5	55.5%
C	2.7–3.3	24.2%
D	3.7–4.3	2.2%
E	4.7–5.3	1.8%
F	5.7–6.3	0.8%
G	8	1.9%



31 December 2009

A	1	20.5%
B	1.7–2.5	51.2%
C	2.7–3.3	20.1%
D	3.7–4.3	1.5%
E	4.7–5.3	1.7%
F	5.7–6.3	1.2%
G	6.7–7.3	3.8%

¹⁶ VaR is a statistical estimate of the maximum probable loss that can be incurred, due to adverse movements in major risk drivers, over a one day trading horizon and estimated at a given confidence level. Expected shortfall, or eVaR, is the average loss beyond the VaR level and is a more accurate measure of large potential losses.

¹⁷ Using the Bank's internal rating scale, where 1.7 is equivalent to an external rating of AA+/Aa1/AA+ with S&P/Moody's/Fitch ratings and 2.0 is equivalent to an external rating of AA/Aa2/AA.

¹⁸ BBB-/Baa3/BBB- level or above.

Placements with and advances to credit institutions

Set out below is an analysis of the Bank's placements with and advances to credit institutions for each of the Bank's relevant internal risk rating categories.

Risk rating	2010 € million	2009 € million
1-3: Excellent to very good	2,802	3,116
4: Good	77	13
5-6: Satisfactory to acceptable	95	118
At 31 December	2,974	3,247

At 31 December 2010 there were no placements with and advances to credit institutions that were past due or impaired (2009: nil).

Debt securities

Risk Management determines the eligibility of credit exposures based on the internal risk ratings applied and the parameters set out in the T&TRMA and other relevant policies and guidelines. In cases where the creditworthiness of security issuers deteriorates to levels below the standard of eligibility for new exposures, Risk Management and Treasury jointly recommend actions for the approval of the Vice President, Risk and Resources and the Vice President, Finance and Chief Financial Officer. Any decision to retain ineligible exposures is reported to the TEC and the Audit Committee.

In cases where the Bank considers the exposure to be permanently reduced in value, impairment for financial assets at amortised cost is recognised in the income statement. Impairment is further discussed under the "Accounting policies" section on page 17.

Debt securities at fair value through profit or loss

Set out below is an analysis of the Bank's debt securities at fair value through profit or loss for each of the Bank's relevant internal risk rating categories. No collateral is held over impaired debt securities.

Risk rating	2010 € million	2009 € million
1-3: Excellent to very good	647	213
4: Good	65	–
5-6: Satisfactory to acceptable	7	9
7-8: Special attention to substandard	18	–
At 31 December	737	222

There were no debt securities at fair value past due in 2010 or 2009.

Debt securities at amortised cost

Set out below is an analysis of the Bank's debt securities at amortised cost for each of the Bank's relevant internal risk rating categories. No comparatives are required upon early adoption of IFRS 9.

Risk rating	Neither past due nor impaired € million	Impaired gross € million	Total € million	Cumulative impairment losses € million	Total net of impairment € million
1-3: Excellent to very good	8,706	–	8,706	–	8,706
4: Good	142	–	142	–	142
5-6: Satisfactory to acceptable	30	–	30	–	30
7-8: Special attention to substandard	–	187	187	(110)	77
At 31 December 2010	8,878	187	9,065	(110)	8,955

Available-for-sale debt securities (applicable to 31 December 2009)

At 31 December 2009, there were no available-for-sale debt securities that were past due or impaired.

Risk rating	2009 € million
1-3: Excellent to very good	1,000
5-6: Satisfactory to acceptable	12
At 31 December	1,012

Derivative financial assets

Set out below is an analysis of the Bank's derivatives for each of the Bank's internal rating categories.

Risk rating	2010 € million	2009 € million
1-3: Excellent to very good	3,628	2,532
4: Good	52	–
5-6: Satisfactory to acceptable	445	6
7-8: Special attention to substandard	40	–
9: Doubtful	3	–
At 31 December	4,168	2,538

There were no derivative financial assets past due in 2010 or 2009.

Treasury loan investments (applicable to 31 December 2009)

Set out below is an analysis of the Bank's Treasury loan investments for each of the Bank's relevant internal risk rating categories.

Risk rating	Neither past due nor impaired € million	Impaired gross € million	Total € million	Cumulative impairment losses € million	Total net of impairment € million
1-3: Excellent to very good	5,010	–	5,010	–	5,010
4: Good	118	–	118	–	118
5-6: Satisfactory to acceptable	76	–	76	–	76
7-8: Special attention to substandard	–	279	279	(162)	117
9: Doubtful	–	1	1	(1)	–
At 31 December 2009	5,204	280	5,484	(163)	5,321

These assets, originally classified as available-for-sale, were reclassified into the category loans and receivables, effective from 1 July 2008.

Derivatives

The Bank's use of exchange-traded and OTC derivatives is primarily focused on hedging interest rate and foreign exchange risks arising from both its Banking and Treasury activities. Market views expressed through derivatives are also undertaken as part of Treasury's activities, while the transactions through which the Bank funds itself in capital markets are typically swapped into floating-rate debt with derivatives. In addition, the Bank uses credit derivatives as an alternative to investments in specific securities or to hedge certain exposures.

The risks arising from derivative instruments are combined with those deriving from all other instruments dependent on the same underlying risk factors, and are subject to overall market and credit risk limits, as well as to stress tests. Additionally, special care is devoted to those risks that are specific to the use of derivatives, through, for example, the monitoring of volatility risk for options, credit spread risk for swaps and basis risk for futures.

The table below shows the fair value of the Bank's derivative financial assets and liabilities at 31 December 2010 and 31 December 2009.

	Assets 2010 € million	Liabilities 2010 € million	Total 2010 € million	Assets 2009 € million	Liabilities 2009 € million	Total 2009 € million
Derivatives held for trading						
OTC foreign currency products						
Currency swaps	117	(91)	26	119	(29)	90
Spot and forward currency transactions	37	(63)	(26)	157	(24)	133
	154	(154)	-	276	(53)	223
OTC interest rate products						
Interest rate swaps	87	(101)	(14)	78	(76)	2
OTC credit products						
Credit default swaps	9	(16)	(7)	9	(24)	(15)
Banking derivatives						
Fair value of equity derivatives held in relation to the Banking portfolio	573	(30)	543	218	(86)	132
Total derivatives held for trading and Banking derivatives	823	(301)	522	581	(239)	342
Derivatives held for hedging						
Derivatives designated as fair value hedges						
Interest rate swaps	948	(301)	647	560	(168)	392
Cross currency interest rate swaps	2,397	(466)	1,931	1,397	(381)	1,016
	3,345	(767)	2,578	1,957	(549)	1,408
Derivatives designated as cash flow hedges						
Forward currency transactions	-	(2)	(2)	-	(15)	(15)
Total derivatives held for hedging	3,345	(769)	2,576	1,957	(564)	1,393
Total derivatives at 31 December	4,168	(1,070)	3,098	2,538	(803)	1,735

In order to manage credit risk in OTC derivative transactions, the Bank's policy is to approve *ex ante* each counterparty individually and to review its creditworthiness and eligibility regularly. Overall limits are allocated to each eligible counterparty in compliance with guidelines that set a maximum for the size and tenor of exposure, based on the counterparty's internal credit rating and outlook. For those counterparties, typically banks, that are deemed eligible for foreign exchange and OTC derivatives, a portion of the overall counterparty limit is allocated to these instruments. Utilisation of limits, whether overall counterparty limits or dedicated foreign exchange and OTC derivatives limits, is calculated using a potential future exposure methodology. This is based on a Monte Carlo simulation-based model and is measured and monitored daily for all counterparties by Risk Management.

OTC derivative transactions are normally carried out only with the most creditworthy counterparties, rated at the internal equivalent of single-A and above. Furthermore, the Bank pays great attention to mitigating the credit risk of OTC derivatives through the negotiation of appropriate legal documentation with counterparties. OTC derivatives transactions are systematically documented with a Master Agreement (MA) and a Credit Support Annex (CSA). These provide for close-out netting and the posting of collateral by the counterparty once the Bank's exposure exceeds a given threshold, which is a function of the counterparty's perceived risk rating.

The Bank has also expanded the scope for applying risk mitigation techniques by documenting the widest possible range of instruments transacted with a given counterparty under a single MA and CSA, notably foreign exchange transactions. The Bank also systematically resorts to unwinding-upon-credit-downgrading clauses and, for long-dated transactions, unilateral break clauses. Similarly, the Bank emphasises risk mitigation for repurchase and reverse repurchase agreements and related transaction types through MA documentation.

At 31 December 2010, 93 per cent (2009: 83 per cent) of the Bank's gross exposure to derivatives counterparties was against counterparties with whom an MA and CSA had been completed, allowing for receipt of collateral in the form of cash or liquid, triple-A-rated government securities.

Collateral

The Bank mitigates credit risk by holding collateral against exposures to derivative counterparties.

Counterparty exposure, for the purposes of collateralising credit risk, is only concerned with counterparties with whom the Bank has an overall net positive exposure. At 31 December 2010 this exposure stood at €2.8 billion (2009: €1.8 billion). Against this, the Bank held collateral of €2.6 billion (2009: €1.6 billion), reducing its net credit exposure to €0.2 billion (2009: €0.2 billion).

Where the Bank borrows or purchases securities subject to a commitment to resell them (a reverse repurchase agreement) but does not acquire the risk and rewards of ownership, the transactions are treated as collateralised loans. The securities are not included in the statement of financial position and are held as collateral.

The table below illustrates the fair value of collateral held that is permitted to be sold or repledged in the absence of default. Sold or repledged collateral includes collateral on-lent through bond lending activities. In all cases the Bank has an obligation to return equivalent securities.

	Held collateral 2010 € million	Sold or repledged 2010 € million	Held collateral 2009 € million	Sold or repledged 2009 € million
Collateral held as security				
Derivative financial instruments				
Triple-A-rated government securities	1,900	-	679	-
Cash	723	723	929	929
Reverse sale and repurchase transactions	1,587	-	1,976	-
At 31 December	4,210	723	3,584	929

The term "collateralised placements" in the Bank's statement of financial position is used to describe the economic substance of the transactions comprising that category. Such transactions involve the purchase of a financial asset together with entering into a total return swap whereby the risks and rewards of ownership of the asset are transferred back to the entity selling the asset. For accounting purposes, therefore, the economic substance of such transactions is a form of collateralised lending. However as the assets are legally owned by the Bank, they do not represent collateral for the purposes of the above disclosure. At 31 December 2010, the Bank held €1.2 billion (2009: €1.2 billion) of collateralised placements.

Credit risk in the Treasury portfolio: Concentration**Concentration by country and region**

At the end of 2010 Treasury credit risk exposure was allocated across 28 countries. The top five countries (by percentage of the total exposure) were the United States (27 per cent), United Kingdom (12 per cent), France (8 per cent), Spain (8 per cent) and the Netherlands (8 per cent). The top five countries at 31 December 2009 were the United States (35 per cent), the Netherlands (12 per cent), United Kingdom (11 per cent), Japan (9 per cent) and Spain (8 per cent).

Concentration by counterparty type

By counterparty type, banks represented the largest portion of the portfolio peak exposure at 66 per cent at 31 December 2010 (2009: 62 per cent). Exposure to counterparties in the countries of operations remained stable at 2 per cent of peak exposure. Sovereign exposure increased to 12 per cent (2009: 9 per cent) and consists mainly of US Treasury bonds posted to the Bank as collateral by OTC derivatives counterparties.

B. MARKET RISK

Market risk is the potential loss that could result from adverse market movements. The drivers of market risk are: (i) interest rate risk; (ii) foreign exchange risk; (iii) equity risk; and (iv) commodity price risk. Interest rate risks are further broken down into yield curve risk, which measures the impact of changes in the position and shape of the yield curve for a given currency, and volatility risk, which deals with risks specific to interest rate option transactions. Yield curve risk can in turn be divided into changes in the overall level of interest rates (a parallel shift of an entire yield curve), and changes in the slope or the shape of the yield curve.

Similarly, foreign exchange rate risks are split into risk emanating from changes in the level of foreign exchange rates and volatility risk, which is inherent within foreign exchange options. In the market risk area, 2010 saw markets with variable risk appetite because of the European sovereign crisis. This led to a higher volatility in currency movements, but equity markets rallied from July onwards. The most significant movements in terms of direct exposure have been those in listed equities (Banking) and foreign exchange. Interest rate exposure is kept to a minimum (relative to the Bank's capital) and only minor movements have been observed.

Concentration of Treasury peak exposure by country/region**31 December 2010**

United States	26.8%
United Kingdom	11.9%
France	8.3%
Spain	8.3%
The Netherlands	7.6%
Japan	6.5%
Denmark	6.3%
Italy	5.4%
Belgium	4.0%
Australia	3.6%
Sweden	2.8%
Germany	2.2%
Canada	1.1%
Russia	1.0%

31 December 2009

United States	35.1%
The Netherlands	11.9%
United Kingdom	10.6%
Japan	9.2%
Spain	7.5%
France	7.2%
Australia	4.1%
Italy	3.9%
Germany	2.6%
Canada	1.5%
Belgium	1.2%
Switzerland	1.1%
Russia	1.0%
Denmark	1.0%

Market risk in the Banking portfolio

The Banking loan portfolio is match-funded by Treasury in terms of currency, so for loan facilities extended in currencies other than euro the foreign exchange risk is hedged via the Treasury portfolio. Likewise, interest rate risk to which the Banking loan portfolio would normally be exposed is managed through the Treasury portfolio. As such there is minimal residual foreign exchange or interest rate risk present in the Banking loan portfolio. The main exposure to market risk in the Banking portfolio arises from the exposure of share investments to foreign exchange and equity price risk, neither of which is captured in the VaR figures discussed under “Market risk in the Treasury portfolio” on page 43. Additional sensitivity information for the Bank’s share investments has been included under “Fair value hierarchy” on page 57.

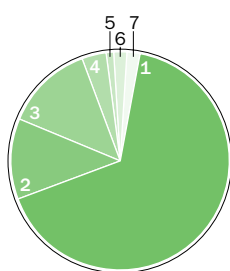
Foreign exchange risk

The tables below summarise the potential impact on the Bank’s net profit and available-for-sale reserves (applicable to 31 December 2009) from a strengthening or weakening of foreign exchange rates relative to the euro.

Share investments at fair value through profit or loss

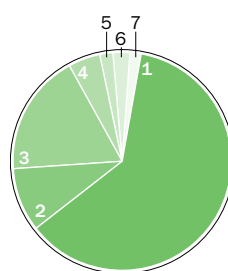
	5 year rolling average movement in exchange rate %	Fair value € million	Impact on net profit € million
Croatian kuna	0.1	450	-
Euro	-	1,486	-
Hungarian forint	2.2	174	4
Kazakhstan tenge	0.5	248	1
Polish zloty	3.7	264	10
Romanian leu	6.4	375	24
Russian rouble	4.0	1,348	54
United States dollar	6.4	693	44
Other non-euro	3.9	760	28
At 31 December 2010	-	5,798	165

Exposure by counterparty type



31 December 2010

1	Banks	66.4%
2	Sovereigns	12.0%
3	Asset-backed-securities	13.0%
4	Insurance companies	3.8%
5	Derivative product companies	1.1%
6	Corporates	1.9%
7	CoO Counterparties	1.8%



31 December 2009

1	Banks	61.7%
2	Sovereigns	9.5%
3	Asset-backed-securities	18.0%
4	Insurance companies	4.9%
5	Derivative product companies	2.0%
6	Corporates	2.4%
7	CoO Counterparties	1.5%

Share investments at fair value through profit or loss

	5 year rolling average movement in exchange rate %	Fair value € million	Impact on net profit € million
Croatian kuna	0.6	316	2
Euro	–	763	–
Hungarian forint	2.1	140	3
Polish zloty	5.5	141	8
Russian rouble	7.3	358	26
United States dollar	7.7	175	13
Other non-euro	5.2	386	20
At 31 December 2009	–	2,279	72

Available-for-sale share investments (applicable to 31 December 2009)

	5 year rolling average movement in exchange rate %	Fair value € million	Impact on available-for- sale reserves (strengthening relative to euro) € million	Impact on net profit (weakening relative to euro) ¹⁹ € million	Impact on available-for- sale reserves (weakening relative to euro) ¹⁹ € million
Croatian kuna	0.6	153	1	–	(1)
Euro	–	561	–	–	–
Hungarian forint	2.1	135	3	–	(3)
Kazakhstan tenge	4.2	230	10	–	(10)
Polish zloty	5.5	143	8	–	(8)
Romanian leu	7.7	298	23	–	(23)
Russian rouble	7.3	432	32	(7)	(25)
United States dollar	7.7	174	13	(3)	(10)
Other non-euro	5.2	329	17	(1)	(16)
At 31 December 2009	–	2,455	107	(11)	(96)

Equity price risk

In terms of equity price risk, the Bank expects the effect on net profit will bear a linear relationship to the movement in equity indices. The table below summarises the potential impact on the Bank's net profit and available-for-sale reserves (applicable to 31 December 2009) from an increase or decrease in relevant benchmark indices.

Share investments at fair value through profit or loss

		5 year rolling average movement in benchmark index %	Fair value € million	Impact on net profit € million
Croatia	CROBEX Index	42.5	450	191
Hungary	CHTX Index	36.0	183	66
Kazakhstan	KASE Index	85.7	252	216
Poland	WIG Index	33.7	308	104
Romania	BET Index	38.4	375	144
Russia	RTS Index	62.7	1,739	1,090
Serbia	BELEX15 Index	63.8	170	108
Slovak Republic	SAX Index	13.4	190	25
Ukraine	PFTS Index	82.3	137	112
Regional and other	Weighted average	54.1	1,994	1,065
At 31 December 2010		–	5,798	3,121

¹⁹ For available-for-sale share investments, the potential impact on net profit and available-for-sale reserves from a weakening of foreign exchange rates relative to the euro has been assessed relative to the Bank's impairment triggers.

		5 year rolling average movement in benchmark index %	Fair value € million	Impact on net profit € million
Croatia	CROBEX Index	47.0	316	148
Hungary	CHTX Index	36.6	148	54
Kazakhstan	KASE Index	125.7	62	78
Poland	WIG Index	36.7	182	67
Russia	RTS Index	74.8	509	381
Serbia	BELEX15 Index	63.2	122	77
Slovak Republic	SAX Index	14.1	–	–
Ukraine	PFTS Index	75.4	60	45
Regional and other	Weighted average	62.4	880	549
At 31 December 2009		–	2,279	1,399

Available-for-sale share investments (applicable to 31 December 2009)

		5 year rolling average movement in benchmark index %	Fair value € million	Impact on available-for-sale reserves (increase in benchmark indices) € million	Impact on net profit (decrease in benchmark indices) ²⁰ € million	Impact on available-for-sale reserves (decrease in benchmark indices) ²⁰ € million
Croatia	CROBEX Index	47.0	153	72	(30)	(42)
Hungary	CHTX Index	36.6	125	46	–	(46)
Kazakhstan	KASE Index	125.7	233	293	(144)	(149)
Poland	WIG Index	36.7	132	49	(11)	(38)
Romania	BET Index	47.3	336	159	–	(159)
Russia	RTS Index	74.8	551	413	(239)	(174)
Serbia	BELEX15 Index	63.2	13	8	(8)	–
Slovak Republic	SAX Index	14.1	117	16	–	(16)
Ukraine	PFTS Index	75.4	39	29	(28)	(1)
Regional and other	Weighted average	62.4	756	472	(295)	(177)
At 31 December 2009		–	2,455	1,557	(755)	(802)

Market risk in the Treasury portfolio

The Bank's market risk exposure arises from the fact that the movement of interest rates and foreign exchange rates may have an impact on positions taken by the Bank.

The Bank monitors its exposure to market risk in its portfolio through a combination of limits, based on Monte Carlo simulation-based eVaR, also known as expected shortfall, and a variety of additional risk measures. The Bank's overall eVaR limit is laid down in the Board-approved T&TRMA. Foreign exchange exposures are further constrained by a dedicated eVaR sub-limit.

Additional eVaR measures are monitored, in particular for drilling down from aggregate eVaR measures to individual market factors (marginal eVaR and VaR sensitivities). For the options portfolio, dedicated options eVaR computations are performed in order to factor in the non-linear behaviour of option instruments.

For internal monitoring purposes, eVaR is defined as the average (above a certain threshold) potential loss that could be incurred due to adverse fluctuations in interest rates and foreign exchange rates over a one-day trading horizon and computed with a 95 per cent confidence level. For enhanced comparability across institutions, numbers disclosed in this financial report are also VaR-based and scaled up to a 99 per cent confidence level over a 10-trading-day horizon.

Although eVaR is a more robust measure of market risk than VaR and is used to measure Treasury portfolio risk, it also remains limited by its historical framework insofar as past market events are not necessarily a perfect predictor of future unfolding scenarios. For these reasons a number of other risk measures are employed to complement eVaR and VaR data, with numbers produced using a different set of assumptions and based on a set of risk factor sensitivities. This is also to ensure that material risks are not ignored

²⁰ For available-for-sale share investments, the potential impact on net profit and available-for-sale reserves from a decline in benchmark indices has been assessed relative to the Bank's impairment triggers.

by focusing on one particular set of risk measures. Foreign exchange risk and the various types of interest rate risks, whether for outright exposures or for options, are monitored with sensitivity-based measures independently for each currency and type of option. A series of stress tests is also produced on a daily basis. These primarily encompass:

- stress-testing the options portfolio for joint large changes in the level of the price of the underlying security and that of volatility
- analysing, for each currency separately, the profit and loss impact of large deformations in the level and shape of the yield curve
- producing stress tests covering the entire Treasury portfolio based on historical scenarios.

This approach is in line with the needs for complementary risk monitoring as evidenced in the recent market turmoil, and will be further strengthened and refined in light of the lessons learnt from the economic crisis.

The Bank aims to limit and manage market risks as far as possible through active asset and liability management. Interest rate risks are managed by synthetically hedging the interest rate profiles of assets and liabilities, mainly through the use of exchange-traded and OTC derivatives for hedging purposes. Exposures to foreign exchange and interest rate risks are measured and monitored daily by Risk Management to ensure compliance with authorised limits. The limits themselves are low compared with the Bank's capital, and in addition to that, actual limit utilisation has been quite low (typically less than 50 per cent). The corresponding profit and loss movements have also been very limited through 2010, illustrating the low risk levels to market risk as specified above.

Interest rate and foreign exchange risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates. The length of time for which the rate of interest is fixed on a financial instrument indicates the extent to which it is exposed to interest rate risk.

The Bank's interest rate risk measurement is complemented by accepted market techniques including VaR, (non-credit) spread risk and volatility risk, on which frequent management reporting takes place.

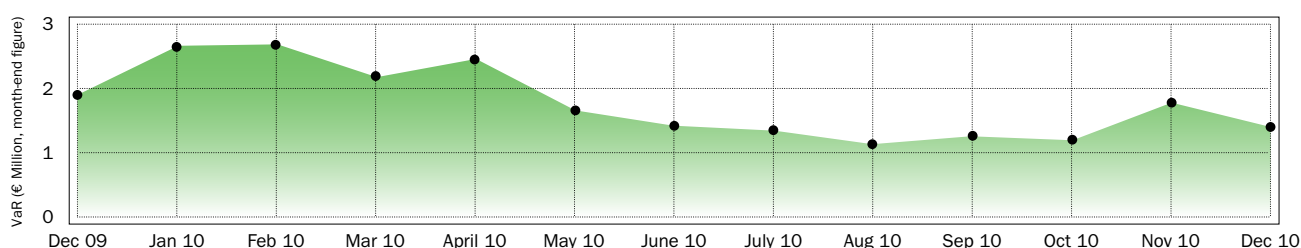
At 31 December 2010, the aggregate VaR of the Bank's Treasury portfolio, calculated by reference to a 99 per cent confidence level and over a ten-trading-day horizon, stood at €1.5 million (2009: €2.0 million). Correlation effects in the portfolio reduce the aggregate VaR below the sum of the individual VaR exposures.

The month-end VaR attained its maximum of €2.7 million at the end of February, well within the Board-approved total VaR limit for all Treasury funds.²¹ The average VaR over the year was €1.8 million (2009: €5.9 million), while the lowest and highest values were €1.1 million and €2.7 million respectively (2009: €1.8 million and €11.6 million).

Market risk exposure incurred by Treasury derives mainly from positions managed internally by Treasury.²² Within the overall market risk exposure, the VaR of the internally managed portfolios stood at €1.5 million at the end of 2010 (2009: €2.0 million). The range during the year was between €0.7 million and €3.1 million (2009: between €1.3 million and €7.2 million). The size of the internally managed portfolio to which these figures relate was €11.2 billion at 31 December 2010 (2009: €9.6 billion).

The specific contribution from foreign exchange risk to the overall VaR stood at €0.1 million at year-end (2009: €0.2 million). As in previous years, this contribution was small throughout 2010 and never exceeded €2.4 million (2009: €1.3 million). Interest rate positioning continued to represent the majority of the Bank's market risk exposure. Interest rate option exposure remained modest throughout the year with option VaR at just €0.2 million at year-end (2009: €0.6 million), having peaked at €1.2 million in April (2009: €3.6 million in June).

Total VaR (10 trading days, 99% confidence level, BIS complaint dataset)



²¹ This limit stood at €18 million as of 1 January 2010. The Board approved a 50 per cent increase of the limit to €27 million on 20 July 2010 (BDS10-165).

²² The VaR takes into account Treasury's externally managed portfolio which consists only of cash and short-dated reverse repos, therefore its contribution to the total VaR is minimal.

In addition to the above, the sterling budget hedges portfolio, tied to the EUR/GBP currency movements, had a stand-alone VaR figure of €8.8 million at year-end. Since the portfolio is not actively managed (nor limit-based), it would be inappropriate to combine the VaR figure with other risk measures for the Treasury portfolio.

Equity price risk

The Bank has direct exposure to equity risk through one Treasury share investment for which the market risk is assessed on a stand-alone basis within a VaR/eVaR framework and added to the overall Treasury risk. Indirect exposure to equity risk occurs in the form of linked structures that are traded on a back-to-back basis and therefore result in no outright exposure.

Commodity price risk

At 31 December 2010 the Treasury portfolio was not exposed to any commodity risk as all such transactions had been performed on a back-to-back basis.

C. LIQUIDITY RISK

Liquidity risk management process

The Bank's liquidity policy is set out in the Liquidity Policy Review. This document is updated annually and approved by the Board of Directors. The overall liquidity policy within this document sets out the framework that ensures the Bank's ability to meet all its liquidity obligations in the medium term, with further details incorporated within the liquidity management guidelines as part of the Treasury Guidelines. As part of this annual review process, there is an assessment of the Bank's projected liquidity based on projected operational and financial cash flows, together with the proposed Borrowing Programme for the following year. The Bank's liquidity position is also monitored on a monthly basis by the Vice President, Risk and Resources.

The Bank is committed to maintaining a strong liquidity position. To ensure this, the Bank requires a minimum target liquidity ratio, based on a multi-year context, of 45 per cent of its next three years' net cash requirements, and 75 per cent of all committed but undisbursed project financing plus one year's debt service. This policy is implemented by maintaining liquidity in an operating target zone of 90 per cent of the next three years' net cash requirements, and 100 per cent of committed but undisbursed project financing, plus one year's debt service – above the required minimum level.

For the purposes of the Bank's internal liquidity policies, all assets managed within its Treasury portfolio are considered to represent the Bank's liquidity. On this basis the Bank exceeded the minimum requirement on each of its two key liquidity policies, both at 31 December 2010 and consistently throughout the year.

IFRS 7 – Financial Instruments: Disclosures, requires a maturity analysis of the undiscounted cash flows deriving from the Bank's financial liabilities. Cash flows are presented in the earliest maturity band in which they could potentially fall due. For this purpose, the Bank profiles its callable debt in line with options conferring the right to its derivative counterparties to terminate the associated hedging instruments prior to legal maturity. This reflects how the Bank manages its debt in practice despite the fact that the debt is callable at the option of the Bank and therefore there is no legal obligation to redeem the debt before its legal maturity.

Net settling interest rate derivatives typically include interest rate swaps and forward rate agreements. Gross settling interest rate derivatives include cross currency interest rate swaps. While the pay legs of these derivatives must be disclosed, the inflows have also been presented in the accompanying table for information purposes. Foreign exchange derivatives include currency forwards and currency swaps. As exchange traded interest rate futures and options are cash settled daily, their undiscounted future cash flows at the statement of financial position date are negligible.

As the figures represent undiscounted cash flows, they do not agree to the statement of financial position.

Financial liabilities at 31 December 2010	Up to and including 1 month € million	Over 1 month and up to and including 3 months € million	Over 3 months and up to and including 1 year € million	Over 1 year and up to and including 3 years € million	Over 3 years € million	Total € million
Non-derivative cash flows						
Amounts owed to credit institutions	(1,914)	-	-	-	-	(1,914)
Debts evidenced by certificates	(443)	(902)	(4,020)	(7,122)	(14,696)	(27,183)
Other financial liabilities	-	-	(6)	-	(64)	(70)
At 31 December 2010	(2,357)	(902)	(4,026)	(7,122)	(14,760)	(29,167)
Trading derivative cash flows						
Net settling interest rate derivatives	(2)	(8)	(27)	(41)	(40)	(118)
Gross settling interest rate derivatives – outflow	(5)	(31)	(799)	(1,721)	(266)	(2,822)
Gross settling interest rate derivatives – inflow	3	30	763	1,618	288	2,702
Foreign exchange derivatives – outflow	(1,301)	(951)	(974)	-	-	(3,226)
Foreign exchange derivatives – inflow	1,274	920	962	-	-	3,156
Credit derivatives	-	-	(1)	(2)	-	(3)
At 31 December 2010	(31)	(40)	(76)	(146)	(18)	(311)
Hedging derivative cash flows						
Net settling interest rate derivatives	(4)	(6)	4	(49)	(136)	(191)
Gross settling interest rate derivatives – outflow	(16)	(223)	(454)	(794)	(1,465)	(2,952)
Gross settling interest rate derivatives – inflow	23	183	492	904	1,212	2,814
At 31 December 2010	3	(46)	42	61	(389)	(329)
Total financial liabilities at 31 December 2010	(2,385)	(988)	(4,060)	(7,207)	(15,167)	(29,807)
Other financial instruments						
Undrawn commitments						
Financial institutions	(2,796)	-	-	-	-	(2,796)
Non-financial institutions	(6,598)	-	-	-	-	(6,598)
At 31 December 2010	(9,394)	-	-	-	-	(9,394)

Financial liabilities at 31 December 2009	Up to and including 1 month € million	Over 1 month and up to and including 3 months € million	Over 3 months and up to and including 1 year € million	Over 1 year and up to and including 3 years € million	Over 3 years € million	Total € million
Non-derivative cash flows						
Amounts owed to credit institutions	(2,109)	(23)	–	–	–	(2,132)
Debts evidenced by certificates	(589)	(1,835)	(3,321)	(4,491)	(12,273)	(22,509)
Other financial liabilities	–	–	(59)	–	(65)	(124)
At 31 December 2009	(2,698)	(1,858)	(3,380)	(4,491)	(12,338)	(24,765)
Trading derivative cash flows						
Net settling interest rate derivatives	–	(2)	(29)	(28)	(28)	(87)
Gross settling interest rate derivatives – outflow	(4)	(35)	(113)	(879)	(148)	(1,179)
Gross settling interest rate derivatives – inflow	2	36	113	860	129	1,140
Foreign exchange derivatives – outflow	(558)	(29)	(459)	(55)	–	(1,101)
Foreign exchange derivatives – inflow	542	27	443	50	–	1,062
Credit derivatives	–	(1)	(2)	(5)	(4)	(12)
At 31 December 2009	(18)	(4)	(47)	(57)	(51)	(177)
Hedging derivative cash flows						
Net settling interest rate derivatives	(22)	(17)	(14)	(71)	(105)	(229)
Gross settling interest rate derivatives – outflow	(92)	(419)	(959)	(1,193)	(1,837)	(4,500)
Gross settling interest rate derivatives – inflow	103	430	1,012	1,247	1,634	4,426
At 31 December 2009	(11)	(6)	39	(17)	(308)	(303)
Total financial liabilities at 31 December 2009	(2,727)	(1,868)	(3,388)	(4,565)	(12,697)	(25,245)
Other financial instruments						
Undrawn commitments						
Financial institutions	(2,257)	–	–	–	–	(2,257)
Non-financial institutions	(5,459)	–	–	–	–	(5,459)
At 31 December 2009	(7,716)	–	–	–	–	(7,716)

In practice, the Bank manages its liquidity risk using cash flow forecasts that still assume the earliest possible redemption of liabilities but expected drawdowns of loan commitments. The table below is a maturity profile of the carrying value of assets and liabilities on the statement of financial position. Financial assets that are classified as trading or available-for-sale are profiled in the earliest maturity band as are other assets within the Treasury portfolio that qualify as collateral for borrowing from the European Central Bank or the United States Federal Reserve. This demonstrates that, before factoring in loan commitments, the Bank has a cumulative positive liquidity position in every maturity band. To the extent that draw downs on loan commitments may create any funding gaps, such gaps are managed through raising debt through either the Bank's commercial paper facilities or euro medium-term note programme, or by selling liquid assets.

At 31 December 2010	Up to and including 1 month € million	Over 1 month and up to and including 3 months € million	Over 3 months and up to and including 1 year € million	Over 1 year and up to and including 3 years € million	Over 3 years € million	Maturity undefined € million	Total € million
Financial assets							
Placements with and advances to credit institutions	2,891	83	-	-	-	-	2,974
Debt securities at fair value through profit or loss	553	-	7	28	149	-	737
Debt securities at amortised cost	6,038	513	936	864	604	-	8,955
Collateralised placements	343	-	-	211	625	-	1,179
Derivative financial instruments	11	53	367	946	2,791	-	4,168
Other assets	80	192	66	65	-	122	525
Banking loans at amortised cost	255	494	1,853	2,337	9,674	-	14,613
Banking loans at fair value through profit or loss	-	-	16	15	190	-	221
Banking share investments	-	-	-	-	-	5,798	5,798
Treasury share investments	-	-	-	-	-	56	56
Paid in capital receivable	-	-	-	-	-	16	16
Total financial assets	10,171	1,335	3,245	4,466	14,033	5,992	39,242
Financial liabilities							
Amounts owed to credit institutions	(371)	(1,540)	-	-	-	-	(1,911)
Debts evidenced by certificates	(982)	(1,290)	(3,402)	(5,863)	(11,499)	-	(23,036)
Derivative financial instruments	(43)	(13)	(94)	(243)	(677)	-	(1,070)
Other liabilities	(2)	(188)	-	(65)	(76)	(2)	(333)
Total financial liabilities	(1,398)	(3,031)	(3,496)	(6,171)	(12,252)	(2)	(26,350)
Net liquidity position at 31 December 2010	8,773	(1,696)	(251)	(1,705)	1,781	5,990	12,892
Cumulative net liquidity at 31 December 2010	8,773	7,077	6,826	5,121	6,902	12,892	
Other financial instruments							
Undrawn commitments							
Financial institutions	(2,796)	-	-	-	-	-	(2,796)
Non-financial institutions	(6,598)	-	-	-	-	-	(6,598)
At 31 December 2010	(9,394)	-	-	-	-	-	(9,394)

At 31 December 2009	Up to and including 1 month € million	Over 1 month and up to and including 3 months € million	Over 3 months and up to and including 1 year € million	Over 1 year and up to and including 3 years € million	Over 3 years € million	Maturity undefined € million	Total € million
Financial assets							
Placements with and advances to credit institutions	3,138	94	15	–	–	–	3,247
Collateralised placements	–	–	–	476	695	–	1,171
Debt securities	1,332	524	617	–	–	–	2,473
Derivative financial instruments	44	131	239	266	1,858	–	2,538
Other assets	147	–	199	61	–	76	483
Treasury loans	3,329	49	81	950	912	–	5,321
Banking loans	561	407	1,491	3,803	6,144	–	12,406
Share investments	–	–	–	–	–	4,791	4,791
Paid in capital receivable	–	–	–	–	–	17	17
Total financial assets	8,551	1,205	2,642	5,556	9,609	4,884	32,447
Financial liabilities							
Amounts owed to credit institutions	(2,106)	(23)	–	–	–	–	(2,129)
Debts evidenced by certificates	(585)	(1,718)	(2,846)	(3,586)	(8,980)	–	(17,715)
Derivative financial instruments	(117)	(14)	(108)	(133)	(431)	–	(803)
Other liabilities	(76)	–	(225)	(76)	–	–	(377)
Total financial liabilities	(2,884)	(1,755)	(3,179)	(3,795)	(9,411)	–	(21,024)
Net liquidity position at 31 December 2009	5,667	(550)	(537)	1,761	198	4,884	11,423
Cumulative net liquidity at 31 December 2009	5,667	5,117	4,580	6,341	6,539	11,423	
Other financial instruments							
Undrawn commitments							
Financial institutions	(2,257)	–	–	–	–	–	(2,257)
Non-financial institutions	(5,459)	–	–	–	–	–	(5,459)
At 31 December 2009	(7,716)	–	–	–	–	–	(7,716)

Capital management

The Bank's original authorised share capital was €10.0 billion. Under Resolution No. 59, adopted on 15 April 1996, the Board of Governors approved a doubling of the Bank's authorised capital stock to €20.0 billion.

In accordance with the requirements of Article 5.3 of the Agreement, the Board of Governors reviews the capital stock of the Bank at intervals of not more than five years. At the Annual Meeting in May 2010 the Bank's Board of Governors approved the Fourth Capital Resources Review (CRR4) which established the Bank's strategy for the period 2011 to 2015. This included an analysis of the transition impact and operational activity of the Bank; an assessment of the economic outlook and transition challenges in the region; the formulation of medium-term portfolio development strategy and objectives; and a detailed analysis of the Bank's projected future financial performance and capital adequacy. The review underlined that the Bank relies on a strong capital base and stressed the need for prudent financial policies supporting conservative provisioning, strong liquidity and long-term profitability.

As a result of the assessment of capital requirements in CRR4, in May 2010 the Board of Governors approved a two-step increase in the authorised capital stock of the Bank: an immediate increase in the authorised paid-in shares of €1.0 billion (Resolution No. 126), and an increase in the authorised callable capital shares of €9.0 billion (Resolution No. 128), for an aggregate increase in the authorised capital stock of the Bank of €10.0 billion (collectively referred to as the second capital increase). The increase in callable capital will become effective when subscriptions have been received for at least 50 per cent of the newly authorised callable capital. Subscriptions are to be received on or before 30 April 2011, and the Board of Directors may extend this date to no later than 31 December 2011. The callable shares are subject to redemption in accordance with the terms of Resolution No. 128.

The Bank does not have any other classes of capital.

The Bank's capital usage is guided by statutory and financial policy parameters. Article 12 of the Agreement establishes a 1:1 gearing ratio which limits the total amount of outstanding loans, share investments and guarantees made by the Bank in its countries of operations to the total amount of the Bank's unimpaired subscribed capital, reserves and surpluses. This capital base is defined in the Bank's Prudential Ratios Policy and incorporates unimpaired subscribed capital, the unrestricted general reserves, loan loss reserve, special reserve and adjustments for accumulated specific and general loan impairment provisions and equity losses. This capital base amounted to €26.2 billion at 31 December 2010 (2009: €24.6 billion). Article 12 also limits the total amount of disbursed share investments to the total amount of the Bank's unimpaired paid-in subscribed capital, surpluses and general reserve. The Bank interprets the gearing ratio on a "disbursed" or "operating assets" basis. As at 31 December 2010 the Bank's gearing ratio was 81 per cent (2009: 73 per cent). No capital utilisation limits were breached during the year (2009: nil).

The Bank's statutory measure of capital adequacy under the gearing ratio is supplemented by a risk-based prudential capital adequacy limit under its Economic Capital Policy.

The Bank defines required economic capital as the potential capital losses – both expected and unexpected – it may incur based on probabilities consistent with the Bank's "triple-A" credit rating. The main risk categories assessed under the economic capital framework are credit risk, market risk and operational risk, and the total risk is managed within an available economic capital base that excludes callable capital, while maintaining a prudent capital buffer.

One of the main objectives of the Economic Capital Policy is to manage the Bank's capital within a medium-term planning framework, providing a consistent measurement of capital headroom over time. The Bank's objective is to prevent the need to call on subscribed callable capital and to use only available risk capital including paid-in capital, reserves and provisions. The available economic capital managed by the Bank consists of paid-in capital, the unrestricted general reserves, loan loss reserve, special reserve and strategic reserve, and adjustments for accumulated general loan impairment provisions and equity losses, assessed at the period end. This capital base amounted to €12.5 billion at 31 December 2010 (2009: €11.5 billion).

At 31 December 2010 the ratio of required economic capital to available economic capital was 69 per cent, compared with a policy threshold for this ratio of 90 per cent (2009: 66 per cent). The Bank's risk-based capital under this policy is managed alongside the Bank's statutory capital constraint.

D. FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

Classification and fair value of financial assets and liabilities

Financial assets at 31 December 2010	Carrying amount € million	Fair value € million
<i>Financial assets measured at fair value through profit or loss or fair value through other comprehensive income:</i>		
– Debt securities	737	737
– Derivative financial instruments	4,168	4,168
– Banking loans at fair value through profit or loss	221	221
– Banking portfolio: share investments at fair value through profit or loss	5,798	5,798
– Treasury portfolio: share investments at fair value through other comprehensive income	56	56
	10,980	10,980
<i>Financial assets measured at amortised cost:</i>		
– Placements with and advances to credit institutions	2,974	2,974
– Debt securities	8,955	8,647
– Collateralised placements	1,179	1,118
– Other financial assets	525	525
– Banking loan investments at amortised cost	14,613	14,306
– Paid in capital receivable	16	16
	28,262	27,586
Total financial assets	39,242	38,566

Financial assets at 31 December 2009	Held for trading € million	At fair value through profit or loss € million	Derivatives held for hedging purposes € million	Loans and receivables € million	Available- for-sale € million	Held-to- maturity € million	Carrying amount € million	Fair value € million
Financial assets								
Placements with and advances to credit institutions	–	–	–	3,247	–	–	3,247	3,247
Collateralised placements	–	–	–	1,171	–	–	1,171	1,244
Debt securities	174	48	–	–	1,012	1,239	2,473	2,473
Derivative financial instruments	363	218	1,957	–	–	–	2,538	2,538
Other financial assets	–	4	–	479	–	–	483	483
Banking share investments	–	2,279	–	–	2,455	–	4,734	4,734
Treasury share investments	–	–	–	–	57	–	57	57
Banking loan investments	–	–	–	12,406	–	–	12,406	9,079
Treasury loan investments	–	–	–	5,321	–	–	5,321	5,133
Paid in capital receivable	–	–	–	17	–	–	17	17
Total financial assets	537	2,549	1,957	22,641	3,524	1,239	32,447	29,005

Financial liabilities at 31 December 2010	Held for trading € million	At fair value through profit or loss € million	Derivatives held for hedging purposes € million	Financial liabilities at amortised cost € million	Carrying amount € million	Fair value € million
Amounts owed to credit institutions	-	-	-	(1,911)	(1,911)	(1,911)
Debts evidenced by certificates	-	-	-	(23,036)	(23,036)	(22,748)
Derivative financial instruments	(271)	(30)	(769)	-	(1,070)	(1,070)
Other financial liabilities	-	-	-	(333)	(333)	(333)
Total financial liabilities	(271)	(30)	(769)	(25,280)	(26,350)	(26,062)

Financial liabilities at 31 December 2009	Held for trading € million	At fair value through profit or loss € million	Derivatives held for hedging purposes € million	Financial liabilities at amortised cost € million	Carrying amount € million	Fair value € million
Amounts owed to credit institutions	-	-	-	(2,129)	(2,129)	(2,129)
Debts evidenced by certificates	-	-	-	(17,715)	(17,715)	(17,503)
Derivative financial instruments	(153)	(86)	(564)	-	(803)	(803)
Other financial liabilities	-	-	-	(377)	(377)	(377)
Total financial liabilities	(153)	(86)	(564)	(20,221)	(21,024)	(20,812)

At 31 December 2010, the Bank's statement of financial position approximates to fair value in all financial asset and liability categories, with the exception of debt securities at amortised cost, Banking loan investments at amortised cost and debts evidenced by certificates.

The basis of fair value for debt securities listed in an active market is the quoted bid market price on the statement of financial position date.

The basis of fair value for debt securities that are unlisted or listed in an inactive market is determined using valuation techniques appropriate to the market and industry of each investment. The primary valuation techniques used are quotes from brokerage services and discounted cash flows. Techniques used to support these valuations include industry valuation benchmarks and recent transaction prices.

Banking loan investments whereby the objective of the Bank's business model is to hold these investments to collect the contractual cash flow, and the contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest, are recognised at amortised cost. In assessing the fair value of these loans, discount rates have been determined considering rates at which similar portfolios of loans would be fair valued at under current market conditions.

"Debts evidenced by certificates" represents the Bank's borrowing activities executed through the issuance of commercial paper and bonds. Due to the short-tenor nature of commercial paper, amortised cost approximates fair value.

Classification of financial assets at the date of initial application of IFRS 9

Upon adoption of IFRS 9 on 1 January 2010, the Bank's financial assets have been reclassified from their IAS 39 categories into amortised cost, fair value through profit or loss or fair value through other comprehensive income. This reclassification resulted in the re-measurement and reallocation of some assets on the statement of financial position. The impact on the Bank's statement of financial position was a net increase to reserves of €216 million.

The table on page 53 illustrates the classification and measurement for each class of financial assets at the date of initial application, 1 January 2010.

The Bank does not have any financial assets in the statement of financial position that were previously designated at fair value through profit or loss but are no longer so designated.

	Financial assets at 31 December 2009 (IAS 39)					Financial assets at 1 January 2010 (IFRS 9)					Difference € million	Note
	Held for trading € million	At fair value through profit or loss € million	Held-to-maturity € million	Loans and receivables € million	Available-for-sale € million	Carrying amount € million	At fair value through profit or loss € million	At fair value through comprehensive income € million	At amortised cost € million	Carrying amount € million		
Financial assets												
Placements with and advances to credit institutions	–	–	–	3,247	–	3,247	–	–	3,247	3,247	–	
Collateralised placements	–	–	–	1,171	–	1,171	–	–	1,171	1,171	–	
Debt securities	174	48	1,239	–	1,012	2,473	493	–	7,503	7,996	5,523	1
Derivative financial instruments	363	2,175	–	–	–	2,538	2,688	–	–	2,688	150	2
Other financial assets	–	–	–	483	–	483	–	–	483	483	–	
Banking loan investments	–	–	–	12,406	–	12,406	113	–	11,855	11,968	(438)	3
Treasury loan investments	–	–	–	5,321	–	5,321	–	–	–	–	(5,321)	4
Banking share investments	–	2,279	–	–	2,455	4,734	5,036	–	–	5,036	302	5
Treasury share investments	–	–	–	–	57	57	–	57	–	57	–	6
Paid-in capital receivable	–	–	–	17	–	17	–	–	17	17	–	
Total financial assets	537	4,502	1,239	22,645	3,524	32,447	8,330	57	24,276	32,663	216	

Note 1 – Debt securities

Investments in debt securities previously classified under the IAS 39 classifications – fair value through profit or loss (€222 million), held to maturity (€1.2 billion), and available-for-sale (€1.0 billion), along with the Treasury loans (€5.3 billion) – were reclassified to debt securities held at amortised cost (€7.5 billion) or fair value (€493 million) at 1 January 2010.

The Bank's business model for the previously classified available-for-sale portfolio is to collect the cash flows from the underlying investments. On transition, the Bank assessed the available-for-sale securities on an individual basis, to determine whether they met the contractual cash flow test (being solely payments of principal and interest). Accordingly debt securities in this portfolio that met the amortised cost criteria under IFRS 9 were classified as such. From this assessment €875 million of available-for-sale debt securities were reclassified to amortised cost. The remaining securities, amounting to €155 million, did not meet the amortised cost definition as they contain payments other than principal and interest and accordingly these securities have been classified at fair value through profit or loss. There was a re-measurement difference upon restating the previously classified available-for-sale debt securities to amortised cost due to the reversal of amounts previously recognised in the available-for-sale reserve relating to revaluations in prior periods. During 2010 an additional gain of €13 million was recognised in the income statement due to these changes.

IAS 39				IFRS 9			
Classification	Note	Measurement		Classification	Measurement		
		Fair value € million	Amortised cost € million		Fair value € million	Amortised cost € million	Difference € million
Debt securities							
Available-for-sale		1,012	–	Debt securities at fair value/at amortised cost	155	875	18
Held-to-maturity		–	1,239	Debt securities at amortised cost	–	1,239	–
At fair value through profit or loss		222	–	Debt securities at fair value	222	–	–
		1,234	1,239		377	2,114	18
Treasury loan investments	4			Debt securities at fair value/at amortised cost	116	5,389	
Debt securities at fair value/at amortised cost					493	7,503	

Note 2 – Derivative financial instruments

On transition to IFRS 9, the carrying amount of derivative financial instruments increased by €150 million. This was due to the reclassification of options attached to portage equities of €150 million (Note 3).

Note 3 – Banking loan investments

On transition to IFRS 9 there were reclassification and re-measurement adjustments to Banking loan investments due to portage equities and convertible loans.

Convertible loans are hybrid contracts that contain an embedded derivative. The derivative component was previously bifurcated under IAS 39 and recognised as a separate instrument. At 31 December 2009 the derivative component had a negligible value. Under IFRS 9 all hybrid contracts with financial asset hosts are classified and measured in their entirety. Due to the presence of an embedded derivative, a convertible loan could have cash flows that are not solely payments of principal and interest, and as a result such loans do not qualify for classification at amortised cost under IFRS 9. Therefore on transition these instruments have been re-classified from loans and receivables and derivatives to financial assets at fair value through profit or loss (€113 million).

Portage equity instruments represent an interest in an equity investment where the Bank also has a put option. The put options, which are valid for certain periods, ensure that the equity can be sold to a creditworthy sponsor for a minimum predetermined amount. Under IAS 39 these instruments were in substance considered debt instruments and the Bank classified such instruments as loans and receivables. Under IFRS 9 the form of these arrangements has been considered and given that the payments received do not represent solely payments of principal and interest, these instruments do not meet the requirements for amortised cost classification. Therefore, the equity and option components of these instruments have been re-classified from loans and receivables to financial assets at fair value through profit or loss.

As a result, on 1 January 2010 €551 million of Banking loans at amortised cost were restated to fair value through profit or loss. A measurement difference of €14 million between their fair value and amortised cost was recognised in opening retained earnings. The measurement difference arises due to the re-measurement of the equity investments and options on portage equities to fair value at 1 January 2010. In 2010 net fair value gains related to these investments amounting to €22 million were recognised in the income statement.

IAS 39				IFRS 9				
Classification	Note	Measurement		Classification	Note	Measurement		
		Fair value € million	Amortised cost € million			Fair value € million	Amortised cost € million	Difference € million
Banking loan investments		–	12,406	Banking loans at fair value/ at amortised cost		113	11,855	(438)
				Banking share investments at fair value	5	302	–	302
				Derivatives	2	150	–	150
Banking loans at fair value/at amortised cost						113	11,855	14

Note 4 – Treasury loan investments

Treasury loans represent debt securities that were previously classified as loans and receivables. Some of these securities failed the contractual cash flow test under IFRS 9 and accordingly these securities were reclassified to loans at fair value through profit or loss (€116 million). The debt securities that continue to meet both the contractual cash flow test and the business model test have been classified at amortised cost.

Upon re-classification a measurement difference arose due to the historical treatment of the debt securities. Prior to 1 July 2008, the debt securities were classified as available-for-sale and were recognised at their fair value with revaluations being recorded within equity. The Bank availed of the option to reclassify these debt securities to loans and receivables on 1 July 2008 under an IAS 39 amendment and the fair value of the securities on that date became the revised amortised cost carrying value. IFRS 9 is applied retrospectively and accordingly the Treasury loan portfolio has been re-measured at 1 January 2010 as though amortised cost had always applied. This resulted in an increase in the carrying value of these securities by €184 million which was recognised in opening retained earnings on transition.

IAS 39				IFRS 9				
Classification	Note	Measurement		Classification	Note	Measurement		
		Fair value € million	Amortised cost € million			Fair value € million	Amortised cost € million	Difference € million
Treasury loans		–	5,321	Debt securities at fair value/ at amortised cost	1	116	5,389	184

Note 5 – Banking share investments

Banking share investments that were previously measured at fair value and classified as available-for-sale are now measured at fair value through profit or loss. This is primarily to avoid disclosing the fair value of each investment (which is confidential and price-sensitive) separately in the financial statements which the Bank is required to do if the share investments are measured at fair value through other comprehensive income. As a result, fair value gains of €863 million were reclassified within the Bank's equity from the available-for-sale investments reserve to retained earnings at 1 January 2010. In 2010 net fair value gains of €266 million related to these investments were recognised in the income statement.

IAS 39				IFRS 9			
Classification	Note	Measurement		Classification	Note	Measurement	
Banking share investments		Fair value € million	Amortised cost € million			Fair value € million	Amortised cost € million
Available-for-sale		2,455	–	Banking share investments at fair value through profit or loss		2,455	–
At fair value through profit or loss		2,279	–	Banking share investments at fair value through profit or loss		2,279	–
				Banking share investments at fair value through profit or loss	3	302	–
Banking share investments at fair value						5,036	–

Note 6 – Treasury share investments

Treasury holds a strategic share investment previously classified under available-for-sale (€57 million) that was reclassified to fair value through other comprehensive income (€57 million). There was no change to the value of the investment upon reclassification although the election to present fair value movements through other comprehensive income will prevent any gains – €9 million at 1 January 2010 – from being recycled through the income statement upon de-recognition of the investment. During 2010 no additional gain was reported in the income statement due to these changes.

Fair value hierarchy

IFRS 7 specifies classification of fair values on the basis of a three-level hierarchy of valuation methodologies. The classifications are determined based on whether the inputs used in the measurement of fair values are observable or unobservable. These inputs have created the following fair value hierarchy.

- Level 1 – Quoted prices in active markets for identical assets or liabilities. This level includes listed share investments on exchanges (for example, RTS Stock Exchange, Zagreb Stock Exchange).
- Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices). This level includes debt securities and most derivative products. The sources of inputs include prices available from screen-based services such as Reuters and Bloomberg, broker quotes and observable market data such as interest rates and foreign exchange rates which are used in deriving the valuations of derivative products.
- Level 3 – Inputs for the asset or liability that are not based on observable market data (unobservable inputs). This level includes share investments and debt securities or derivative products for which not all market data is observable.

The table below provides information at 31 December 2010 about the Bank's financial assets and financial liabilities measured at fair value. Financial assets and financial liabilities are classified in their entirety based on the lowest level input that is significant to the fair value measurement.

At 31 December 2010	Level 1 € million	Level 2 € million	Level 3 € million	Total € million
Debt securities	–	540	197	737
Derivative financial instruments	–	3,578	590	4,168
Banking loans	–	–	221	221
Share investments (Banking portfolio)	1,792	–	4,006	5,798
Share investments (Treasury portfolio)	–	56	–	56
Total financial assets at fair value	1,792	4,174	5,014	10,980
Derivative financial instruments	–	(1,029)	(41)	(1,070)
Total financial liabilities at fair value	–	(1,029)	(41)	(1,070)

At 31 December 2009	Level 1 € million	Level 2 € million	Level 3 € million	Total € million
Debt securities:				
At fair value through profit or loss	–	222	–	222
Available-for-sale	–	857	155	1,012
Derivative financial instruments	–	2,304	234	2,538
Share investments:				
At fair value through profit or loss (Banking portfolio)	362	–	1,917	2,279
Available-for-sale (Banking portfolio)	1,079	–	1,376	2,455
Available-for-sale (Treasury portfolio)	–	57	–	57
Total financial assets at fair value	1,441	3,440	3,682	8,563
Derivative financial instruments	–	(707)	(96)	(803)
Total financial liabilities at fair value	–	(707)	(96)	(803)

There have been no transfers between Level 1 and Level 2 during the year.

The table below provides a reconciliation of the fair values of the Bank's Level 3 financial assets and financial liabilities for the year ended 31 December 2010:

Year ended 31 December 2010	Level 3 financial assets and financial liabilities						
	Debt securities € million	Derivative financial instruments € million	Banking loans € million	Banking share investments € million	Total assets € million	Derivative financial instruments € million	Total liabilities € million
Balance at 31 December 2009	155	234	-	3,293	3,682	(96)	(96)
IFRS 9 reclassification	-	150	113	302	565	-	-
Balance at 1 January 2010	155	384	113	3,595	4,247	(96)	(96)
Total gains/(losses) for the year ended 31 December 2010 in:							
Net (loss)/profit ²³	(5)	221	(4)	108	320	57	57
Purchases/issues	-	-	138	801	939	(2)	(2)
Sales/settlements	(37)	(15)	(26)	(408)	(486)	-	-
Transfers in/(out) of Level 3	84	-	-	(90)	(6)	-	-
Balance at 31 December 2010	197	590	221	4,006	5,014	(41)	(41)
Total gains/(losses) for the period included in net profit for assets and liabilities held at 31 December 2010	10	216	(4)	367	589	57	57

	Level 3 financial assets and financial liabilities					
Year ended 31 December 2009	Debt securities € million	Derivative financial instruments € million	Banking share investments € million	Total assets € million	Derivative financial instruments € million	Total liabilities € million
Balance at 31 December 2008	138	310	3,475	3,923	(16)	(16)
Total gains/(losses) for the year ended 31 December 2009 in:						
Net loss ²⁴	–	(11)	(628)	(639)	(81)	(81)
Other comprehensive income	19	–	(47)	(28)	–	–
Purchases/issues	–	–	751	751	–	–
Sales/settlements	(2)	(65)	(120)	(187)	1	1
Transfers in/(out) of Level 3	–	–	(138)	(138)	–	–
Balance at 31 December 2009	155	234	3,293	3,682	(96)	(96)
Total gains/(losses) for the period included in net loss for assets and liabilities held at 31 December 2009	19	(13)	(652)	(646)	(80)	(80)

²³ Included within the net profit on derivative financial instruments is a loss of €174 million relating to counterparty credit valuation adjustment.

²⁴ Included within the net loss on derivative financial instruments is a loss of €26 million relating to counterparty credit valuation adjustment.

Level 3 – sensitivity analysis

The table below presents the Level 3 financial instruments carried at fair value at 31 December 2010, main valuation models/techniques used in the valuation of these financial instruments and reasonably possible increases or decreases in fair value based on reasonably possible alternative assumptions.

Assets	Main valuation models/techniques	Carrying amount € million	Impact on net profit in 2010	
			Favourable change € million	Unfavourable change € million
Debt securities	Broker quotes and observable market data	197	10	(2)
Derivative financial instruments	Discounted cash flow models	17	-	(3)
Banking derivatives	NAV multiples, EBITDA multiples, discount cash flow models, compounded interest	573	37	(98)
Banking loans	Discount cash flow and option pricing models	221	14	(49)
Banking share investments	NAV multiples, EBITDA multiples, discount cash flow models	4,006	256	(688)
At 31 December		5,014	317	(840)

Liabilities	Main valuation models/techniques	Carrying amount € million	Impact on net profit in 2010	
			Favourable change € million	Unfavourable change € million
Derivative financial instruments	Discounted cash flow models	(11)	-	(2)
Banking derivatives	NAV multiples, EBITDA multiples, discount cash flow models, compounded interest	(30)	2	(5)
At 31 December		(41)	2	(7)

Note: NAV – net asset value; EBITDA – earnings before interest, tax, depreciation and amortisation.

Assets	Main valuation models/techniques	Carrying amount € million	Impact on net profit in 2009		Impact on equity in 2009	
			Favourable change € million	Unfavourable change € million	Favourable change € million	Unfavourable change € million
Debt securities	Broker quotes and observable market data	155	-	(2)	-	-
Derivative financial instruments	Discounted cash flow models	16	-	(5)	-	-
Banking derivatives	NAV multiples, EBITDA multiples, discount cash flow models, compounded interest	218	21	(15)	-	-
Share investments designated at fair value through profit or loss	NAV multiples, EBITDA multiples, discount cash flow models	1,917	200	(142)	-	-
Available-for-sale unlisted equities	NAV multiples, EBITDA multiples, discount cash flow models	1,376	-	(15)	121	(66)
At 31 December		3,682	221	(179)	121	(66)

Liabilities	Main valuation models/techniques	Carrying amount € million	Impact on net profit in 2009		Impact on equity in 2009	
			Favourable change € million	Unfavourable change € million	Favourable change € million	Unfavourable change € million
Banking derivatives	NAV multiples, EBITDA multiples, discount cash flow models, compounded interest	(86)	8	(6)	-	-
At 31 December		(86)	8	(6)	-	-

Treasury debt securities and derivative financial instruments

The Bank's derivative instruments are valued through discounted cash flow models. Valuations are reconciled to counterparty statements on a monthly basis. Therefore the reasonable possible alternative valuations have been determined based on the range of discrepancies between the Bank's valuations and those of our counterparties.

A majority of the Bank's debt securities are priced via a third party market data service, screen-based services such as Reuters and Bloomberg or using broker quotes. For the few debt securities where an active market does not exist, reasonable, alternative valuations have been derived from discounted cash flow models or reasonable adjustments to similarly priced assets.

Banking loans

Banking loans at fair value through profit or loss mainly comprise convertible loans. The valuation models/techniques used to fair value these instruments are discounted cash flow models and option pricing models. The inputs into the models include interest rates, the borrower's credit spreads and underlying equity prices. Reasonable possible alternative valuations have been determined based on the borrower's probability of default.

Banking share investments and derivatives

The Bank's unlisted equity portfolio comprises direct share investments, equity derivatives and equity funds. The main valuation models/techniques used to fair value these financial instruments are net asset value (NAV) multiples, earnings before interest, tax, depreciation and amortisation (EBITDA) multiples and discounted cash flow (DCF) models.

NAV multiples are most commonly applied to bank investments and equity funds. Reasonable possible alternative valuations have been determined based on the NAV multiple ranges in the valuations received for bank investments, and by considering the impact of adjusting the portfolio discount applied to equity funds. For investments valued using EBITDA multiples and DCF models, sensitivity analyses have been performed for the largest investments using reasonable possible alternative assumptions for each investment (for example, increase or decrease in the discount rate).

Notes to the financial statements

1. ESTABLISHMENT OF THE BANK

i Agreement Establishing the Bank

The European Bank for Reconstruction and Development ("the Bank"), whose principal office is located in London, is an international organisation formed under the Agreement Establishing the Bank dated 29 May 1990 ("the Agreement"). At 31 December 2010, the Bank's shareholders comprised 61 countries, together with the European Union (EU) and the European Investment Bank (EIB).

ii Headquarters Agreement

The status, privileges and immunities of the Bank and persons connected with the Bank in the United Kingdom are confirmed and supplemented in the Headquarters Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Bank ("Headquarters Agreement"). The Headquarters Agreement was signed in London at the start of the Bank's operations on 15 April 1991.

2. SEGMENT INFORMATION

The Bank's activities are primarily Banking and Treasury. Banking activities represent investments in projects that, in accordance with the Agreement, are made for the purpose of assisting the countries of operations in their transition to a market economy, while applying sound banking principles. The main investment products are loans, share investments and guarantees. Treasury activities include raising debt finance, investing surplus liquidity, managing the Bank's foreign exchange and interest rate risks and assisting clients in asset and liability management matters.

The Bank's remaining business activities support the Banking and Treasury functions. Information on the financial performance of Banking and Treasury operations is prepared regularly and provided to the chief operating decision-maker. On this basis, Banking and Treasury operations have been identified as the operating segments.

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker, who is responsible for allocating resources and assessing the performance of the operating segments, is the President.

Segment performance

The President assesses the performance of the operating segments based on the net profit for the year, which is measured in a manner consistent with the financial statements.

The segment information provided to the President for the operating segments for the year ended 31 December 2010 and 31 December 2009 is as follows:

	Banking 2010 € million	Treasury 2010 € million	Aggregated 2010 € million	Banking 2009 € million	Treasury 2009 € million	Aggregated 2009 € million
Interest income	645	131	776	648	240	888
Other income/(expense)	928	50	978	(734)	87	(647)
Total segment revenue/(expense)	1,573	181	1,754	(86)	327	241
Less interest expense and similar charges ²⁵	(199)	(57)	(256)	(365)	(173)	(538)
Allocation of the return on capital	87	10	97	209	23	232
Less general administrative expenses	(214)	(14)	(228)	(206)	(14)	(220)
Less depreciation and amortisation	(21)	(1)	(22)	(16)	(1)	(17)
Segment result before provisions and hedges	1,226	119	1,345	(464)	162	(302)
Fair value movement on non-qualifying and ineffective hedges	6	(68)	(62)	121	2	123
Provisions for impairment of loan investments	94	–	94	(535)	(32)	(567)
Net profit/(loss) for the year	1,326	51	1,377	(878)	132	(746)
Transfers of net income approved by the Board of Governors			(150)			(165)
Net profit/(loss) after transfers approved by the Board of Governors			1,227			(911)
Segment assets²⁶	21,558	17,753	39,311	17,660	14,862	32,522
Paid-in capital receivable			16			17
Total assets			39,327			32,539
Segment liabilities						
Total liabilities	168	26,182	26,350	210	20,814	21,024

Segment revenues – Geographic

The Bank's activities are divided into five regions for internal management purposes.

Risk rating	Segment revenue 2010 € million	Segment revenue 2009 € million
Advanced countries ²⁷	267	(60)
Early/intermediate countries ²⁸	460	37
Russia	830	(67)
Turkey	16	4
OECD (Treasury operations)	181	327
Total	1,754	241

Revenues are attributed to countries on the basis of the location in which a project operates.

There were no revenues deriving from transactions with a single external customer that amounted to 10 per cent or more of the Bank's revenues.

²⁵ The Bank's internal interest expense is determined by the rates at which Treasury can borrow funds on the external market. Interest expense is charged to Banking either at a benchmark rate of return for equity investments or at the appropriate base rate for loan investments.

²⁶ The amounts provided to the President with respect to total assets and total liabilities are measured in a manner consistent with that of the financial statements. Assets and liabilities are allocated based on the operations of the segment. Non-segment specific assets and liabilities are allocated on the basis of staff costs.

²⁷ Advanced countries are Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic and Slovenia.

²⁸ Early/intermediate countries are Albania, Armenia, Azerbaijan, Belarus, Bosnia and Herzegovina, Bulgaria, Former Yugoslav Republic (FYR) of Macedonia, Georgia, Kazakhstan, Kyrgyz Republic, Moldova, Mongolia, Montenegro, Romania, Serbia, Tajikistan, Turkmenistan, Ukraine and Uzbekistan.

3. NET INTEREST INCOME

	2010 € million	2009 € million
Interest and similar income		
Banking loans	645	648
Debt securities	95	53
Treasury loans	-	104
Collateralised placements	-	21
Reverse repurchase agreements	8	13
Cash and short-term funds	16	33
Other	12	16
Interest and similar income	776	888
Interest expense and similar charges		
Debts evidenced by certificates	(91)	(287)
Other	(68)	(19)
Interest expense and similar charges	(159)	(306)
Net interest income	617	582

Interest income accrued on impaired financial assets at 31 December 2010 was €0.3 million (2009: €0.1 million).

4. NET FEE AND COMMISSION INCOME

The main components of net fee and commission income are as follows:

	2010 € million	2009 € million
Trade finance fees	9	4
Syndication and agency fees	5	2
Repayment fees	3	2
Administration fees	2	4
Other	2	4
Donor fund expenses	(2)	(2)
Net fee and commission income	19	14

Front-end and commitment fees of €112 million (2009: €120 million) received in 2010, together with related direct costs of €7 million (2009: €9 million), have been deferred on the statement of financial position. They will be recognised in interest income over the period from disbursement to repayment of the related loan, in accordance with IAS 18. In 2010, €39 million (2009: €29 million) of previously deferred fees and direct costs were recognised in interest income.

5. NET GAINS/(LOSSES) FROM SHARE INVESTMENTS AT FAIR VALUE THROUGH PROFIT OR LOSS

	2010 € million	2009 € million
Net realised gains from share investments and equity related derivatives	338	83
Net unrealised gains/(losses) from share investments and equity related derivatives	217	(630)
Net unrealised gains on available-for-sale share investments now measured at fair value through profit or loss upon adoption of IFRS 9	266	–
Net unrealised gains on portage equities reclassified at fair value through profit or loss upon adoption of IFRS 9	29	–
Net gains/(losses) from share investments at fair value through profit or loss	850	(547)

6. NET LOSSES FROM AVAILABLE-FOR-SALE SHARE INVESTMENTS*(applicable to 31 December 2009)*

	2009 € million
Net realised gains from available-for-sale share investments	15
Reversal of previously recognised impairment losses due to sale of share investments or cash recoveries	75
Impairment losses from available-for-sale share investments	(331)
Net losses from available-for-sale share investments	(241)

7. NET LOSSES FROM LOANS AT FAIR VALUE THROUGH PROFIT OR LOSS

	2010 € million
Net unrealised losses from changes in fair value	(7)
Net losses from loans at fair value through profit or loss	(7)

No comparatives are provided upon early adoption of IFRS 9.

8. NET GAINS FROM TREASURY ASSETS HELD AT AMORTISED COST

	2010 € million
Net realised gains from debt securities	1
Recoveries of previously recognised impairments on debt securities	10
Impairment losses from debt securities	(1)
Net gains from Treasury assets held at amortised cost	10

During the year the Bank sold €237 million of debt securities held at amortised cost. These securities were sold in line with Treasury's investment policy to rebalance the duration of the portfolio by investing in longer dated securities or to reduce credit exposures with counterparties. No comparatives are provided upon early adoption of IFRS 9.

9. NET LOSSES FROM TREASURY INVESTMENTS

(applicable to 31 December 2009)

	2009 € million
Realised losses from available-for-sale Treasury assets	(1)
Realised losses on Treasury loans	(8)
Impairment losses from available-for-sale Treasury assets	–
Net losses from Treasury investments	(9)

10. NET GAINS FROM DEALING ACTIVITIES AT FAIR VALUE THROUGH PROFIT OR LOSS

	2010 € million	2009 € million
Debt buy-backs and termination of related derivatives	24	13
Internally managed dealing portfolio held for trading	25	46
Internally managed dealing portfolio designated at fair value through profit or loss	–	23
Internally managed non-dealing debt securities at fair value	(11)	–
Externally managed dealing portfolio designated at fair value through profit or loss	2	13
Net gains from dealing activities at fair value through profit or loss	40	95

Net gains on the dealing portfolio include both realised and unrealised gains or losses, together with associated interest income and expense.

11. OTHER (LOSSES)/GAINS

Other (losses)/gains comprise the fair value movement on non-qualifying and ineffective hedges, as well as foreign exchange gains or losses. For the year, the Bank had a foreign exchange loss of €1 million (2009: gain of €1 million).

The hedging practices and accounting treatment are disclosed under “Derivative financial instruments and hedge accounting” in the Accounting policies on page 20.

Fair value movement on non-qualifying and ineffective hedges

The fair value movement on non-qualifying and ineffective hedges represents an accounting adjustment in respect of hedging relationships undertaken by the Bank that either do not qualify for hedge accounting or do not fully offset when measured in accordance with IFRS. This unrealised adjustment does not reflect economic substance, inasmuch as the reported losses would not be realised in cash were the hedging relationships to be terminated. The adjustment will reverse over time as the underlying deals approach their maturities.

The Bank applies hedge accounting where there is an identifiable, one-to-one relationship between a hedging derivative instrument and a hedged cash instrument. These relationships predominantly arise within the context of the Bank's borrowing activities in which the Bank's issued bonds are combined with swaps to achieve floating-rate debt in the currency sought by the Bank. While such hedges are matched in cash flow terms, accounting rules may require different valuation methodologies to be applied to such cash flows. In particular, a pricing component of currency swaps (known as the basis swap spread) is not applied to the related hedged bond. This component is a feature of supply and demand requirements for other currencies relative to the US dollar or euro. Such differences can create hedge ineffectiveness or hedge failures under IFRS, the combined effect of which is reported within this line of the income statement. For the year this resulted in a net loss of €55 million (2009: gain of €18 million), comprising gains of €1.1 billion (2009: gain of €276 million) on the derivative hedging instruments and losses of €1.2 billion (2009: loss of €258 million) on the hedged items.

In addition to the one-to-one hedge relationships for which the Bank applies hedge accounting, the Bank also hedges interest rate risk across total assets and liabilities on a portfolio basis, for which hedge accounting is not applied. This activity results in the gains or losses arising on the hedging derivative instruments being recognised in the periods in which they occur, while the offsetting impact deriving from the hedged cash instruments will accrue over a different timescale in keeping with the interest rates applicable to the specific periods for those instruments. For the year this resulted in a loss of €13 million (2009: loss of €29 million).

In July 2008, in anticipation of falling interest rates for the euro, the Bank's Executive Committee approved a hedging strategy to lock in the interest rate return on the investment of the Bank's capital until 2010. This was achieved through positions taken in exchange-traded futures contracts. Initially approximately 50 per cent of the Bank's capital was hedged with a further 25 per cent added in December 2008. All remaining contracts were closed out by January 2010. This activity does not, however, qualify for hedge accounting. Therefore the impact of interest rate changes is immediately reflected in the price changes of the futures contracts and reported in the income statement as those prices change. The offsetting changes in the investment return achieved on the Bank's capital is, however, only captured on an accruals basis over time and so will be reflected in the Bank's income statement in future reporting periods. The Bank had recorded a gain of €7 million in 2010 (2009: gain of €134 million) on the futures contracts.

The combined effect of all the hedging activities described above was a loss of €61 million for the year (2009: gain of €123 million).

Cash flow hedges

The Bank hedges on an annual basis to minimise the exchange rate risk associated with incurring administrative expenses in sterling. In 2010 and 2009 there was no ineffectiveness recognised in the income statement arising from cash flow hedges.

12. PROVISIONS FOR IMPAIRMENT OF BANKING LOAN INVESTMENTS AT AMORTISED COST

	2010 € million	2009 € million
Release/(charge) for the year		
Portfolio provisions for the unidentified impairment of loan investments:		
Non-sovereign loan investments	118	(357)
Sovereign loan investments	-	(7)
Specific provisions for the identified impairment of loan investments ²⁹	(24)	(171)
Provisions for impairment of Banking loan investments at amortised cost	94	(535)

	2010 € million	2009 € million
Movement in provisions		
At 1 January	(719)	(227)
Release/(charge) for the year to the income statement	94	(535)
IFRS 9 release of prior year provisions for portage equities and loans at fair value through profit or loss	20	-
Unwinding of the discount relating to the identified impairment of assets	7	3
Foreign exchange adjustments	(39)	11
Charge against amounts written off	7	29
At 31 December	(630)	(719)

	2010 € million	2009 € million
Analysed between		
Portfolio provisions for the unidentified impairment of loan investments:		
Non-sovereign loan investments	(378)	(491)
Sovereign loan investments	(12)	(12)
Specific provisions for the identified impairment of loan investments	(240)	(216)
At 31 December	(630)	(719)

²⁹ During the year, new specific provisions for the identified impairment of loan investments of €112 million (2009: €209 million) were made and €88 million (2009: €38 million) were released or recovered. This resulted in a net charge to the income statement of €24 million (2009: €171 million).

13. PROVISIONS FOR IMPAIRMENT OF TREASURY LOAN INVESTMENTS

(applicable to 31 December 2009)

	2009 € million
Specific provisions for the identified impairment of Treasury loan investments	(32)
Provisions for impairment of Treasury loan investments	(32)

14. GENERAL ADMINISTRATIVE EXPENSES

	2010 € million	2009 € million
Personnel costs	(160)	(157)
Overhead expenses	(75)	(72)
General administrative expenses	(235)	(229)
Release of deferral of direct costs related to loan origination and commitment maintenance	7	9
Net general administrative expenses	(228)	(220)

Sterling general administrative expenses totalled £200 million (2009: £192 million).³⁰

The average number of staff included in personnel costs during the year were: 1,156 Headquarters staff (2009: 1,120); 353 locally hired staff in Resident Offices (2009: 330); 125 contract staff, comprising special employees, interns/short-term staff and locally hired general service contract staff (2009: 110); and 75 Board of Directors personnel (2009: 74). Some 62 staff members were externally funded (2009: 57).

Staff numbers at 31 December 2010 consisted of: 1,172 Headquarters staff (comprising regular and fixed-term staff in Bank departments and Board support staff) (2009: 1,140); 354 locally hired staff in Resident Offices (2009: 352); 128 contract staff (2009: 121), comprising 27 special employees (2009: 26), 75 interns/short-term staff (2009: 68) and 26 locally hired general service contract staff (2009: 27); and 77 Board of Directors personnel (2009: 72). Some 61 staff members were externally funded (2009: 62).

Direct costs of €7 million (2009: €9 million) relating to loan origination in 2010, together with front-end and commitment fee receipts of €112 million (2009: €120 million), have been deferred on the statement of financial position in accordance with IAS 18. These figures will be recognised in interest income over the period from disbursement to repayment of the related loans.

The following fees for work performed by the Bank's external auditors were included in overhead expenses:

	2010 € 000	2009 € 000
Audit and assurance services		
Services as auditors of the Bank	(262)	(237)
Internal controls framework assurance	(135)	(122)
Retirement plan audit	(23)	(21)
Tax recovery audit	(8)	(7)
Audit and assurance services	(428)	(387)

³⁰ Excludes depreciation.

15. PLACEMENTS WITH AND ADVANCES TO CREDIT INSTITUTIONS

	2010 € million	2009 € million
<i>Analysed between</i>		
Current	2,974	3,247
Non-current	–	–
At 31 December	2,974	3,247

“Current” is defined as those assets maturing, or liabilities due, within the next 12 months. All other assets or liabilities are “non-current”.

16. DEBT SECURITIES

	2010 € million	2009 € million
Dealing portfolio at fair value through profit or loss		
Internally managed dealing portfolio held for trading	228	174
Internally managed non-dealing debt securities	211	–
Externally managed dealing portfolio	298	48
At 31 December	737	222
Debt securities at amortised cost		
Debt securities	8,955	–
At 31 December	8,955	–
Available-for-sale		
Available-for-sale portfolio	–	1,012
At 31 December	–	1,012
Held-to-maturity		
Held-to-maturity debt securities	–	1,239
At 31 December	–	2,473
Debt securities at 31 December	9,692	2,473
<i>Analysed between</i>		
Current	8,047	1,917
Non-current	1,645	556
Debt securities at 31 December	9,692	2,473

	2010 € million
Cumulative impairment losses	
Carried forward balance	–
Impairment losses reclassified to amortised cost under IFRS 9	118
Balance at 1 January	118
Release for the year	(9)
Foreign exchange movements	1
At 31 December	110

17. COLLATERALISED PLACEMENTS

<i>Analysed between</i>	2010 € million	2009 € million
Current	343	–
Non-current	836	1,171
At 31 December	1,179	1,171

18. OTHER FINANCIAL ASSETS

	2010 € million	2009 € million
Fair value of derivatives designated as fair value hedges	3,345	1,957
Fair value of derivatives held for trading	250	363
Fair value of derivatives held in relation to the Banking portfolio	573	218
Externally managed funds at fair value through profit or loss	–	4
Interest receivable	192	158
Other	333	321
At 31 December	4,693	3,021

<i>Analysed between</i>	2010 € million	2009 € million
Current	769	760
Non-current	3,924	2,261
At 31 December	4,693	3,021

19. TREASURY LOAN INVESTMENTS

(applicable to 31 December 2009)

Loans and receivables	2009 € million
Loans and receivables	5,484
Less cumulative impairment losses	(163)
At 31 December	5,321

<i>Analysed between</i>	
Current	344
Non-current	4,977
At 31 December	5,321

Cumulative impairment losses	2009 € million
Balance at 1 January	(134)
Charge for the year	(32)
Foreign exchange movements	3
At 31 December	(163)

20. BANKING LOAN INVESTMENTS AT AMORTISED COST

	2010 Sovereign loans € million	2010 Non-sovereign loans € million	2010 Total loans € million	2009 Sovereign loans € million	2009 Non-sovereign loans € million	2009 Total loans € million
Operating assets						
At 31 December 2009	2,264	10,861	13,125	–	–	–
IFRS 9 reclassification	–	(571)	(571)	–	–	–
At 1 January	2,264	10,290	12,554	2,068	8,862	10,930
Movement in fair value revaluation ³¹	–	19	19	–	9	9
Disbursements	358	6,067	6,425	539	5,551	6,090
Repayments and prepayments	(337)	(3,813)	(4,150)	(302)	(3,324)	(3,626)
Foreign exchange movements	68	398	466	(26)	(141)	(167)
Movement in net deferral of front end fees and related direct costs	(12)	(52)	(64)	(15)	(67)	(82)
Written off	–	(7)	(7)	–	(29)	(29)
At 31 December	2,341	12,902	15,243	2,264	10,861	13,125
Impairment at 31 December	(12)	(618)	(630)	(12)	(707)	(719)
Total operating assets net of impairment at 31 December	2,329	12,284	14,613	2,252	10,154	12,406
<i>Analysed between</i>						
Current			2,602			2,459
Non-current			12,011			9,947
Total operating assets net of impairment at 31 December			14,613			12,406

At 31 December 2010 the Bank categorised 46 loans as impaired, with operating assets totalling €465 million (2009: 34 loans totalling €305 million).

21. BANKING LOAN INVESTMENTS AT FAIR VALUE THROUGH PROFIT OR LOSS

	2010 € million
Non-sovereign loans	
At 1 January	113
Disbursements	138
Repayments and prepayments	(26)
Movement in fair value revaluation	(7)
Foreign exchange movements	6
Movement in net deferral of front end fees and related direct costs	(3)
Fair value at 31 December	221
<i>Analysed between</i>	
Current	16
Non-current	205
At 31 December	221

³¹ The movement in fair value revaluation relates to those fixed rate loans that form part of a qualifying hedge relationship with a derivative position and as such are re-measured to fair value in respect of interest rate risk.

22. SHARE INVESTMENTS

	Fair value through profit or loss unlisted share investments € million	Fair value through profit or loss listed share investments € million	Fair value through profit or loss total share investments € million	Available- for-sale unlisted share investments € million	Available- for-sale listed share investments € million	Available- for-sale total share investments € million	Total share investments € million
Outstanding disbursements							
At 31 December 2008	1,452	268	1,720	1,223	966	2,189	3,909
Transfer between classes ³²	(11)	11	–	(3)	3	–	–
Disbursements	486	–	486	230	94	324	810
Disposals	(37)	–	(37)	(62)	(79)	(141)	(178)
Written off	(15)	–	(15)	(6)	–	(6)	(21)
At 31 December 2009	1,875	279	2,154	1,382	984	2,366	4,520
IFRS 9 reclass for portage equities ³³	403	7	410	–	–	–	410
Balance transferred from AFS ³³	1,382	984	2,366	(1,382)	(984)	(2,366)	–
At 1 January 2010	3,660	1,270	4,930	–	–	–	4,930
Transfer from unlisted to listed	(147)	147	–	–	–	–	–
Disbursements	800	128	928	–	–	–	928
Disposals	(380)	(14)	(394)	–	–	–	(394)
Written off	(25)	(2)	(27)	–	–	–	(27)
At 31 December 2010	3,908	1,529	5,437	–	–	–	5,437
Fair value adjustment							
At 31 December 2008	534	56	590	115	(250)	(135)	455
Transfer between classes ³²	–	–	–	(1)	1	–	–
Movement in fair value revaluation	(506)	41	(465)	(4)	484	480	15
Impairment of available-for-sale share investments	–	–	–	(167)	(89)	(256)	(256)
At 31 December 2009	28	97	125	(57)	146	89	214
IFRS 9 reclass for portage equities ³³	(105)	(3)	(108)	–	–	–	(108)
Balance transferred from AFS ³³	(57)	146	89	57	(146)	(89)	–
At 1 January 2010	(134)	240	106	–	–	–	106
Transfer from unlisted to listed	60	(60)	–	–	–	–	–
Movement in fair value revaluation	86	169	255	–	–	–	255
At 31 December 2010	12	349	361	–	–	–	361
Fair value at 31 December 2010	3,920	1,878	5,798	–	–	–	5,798
Fair value at 31 December 2009	1,903	376	2,279	1,325	1,130	2,455	4,734

At 1 January 2010, share investments not held for trading that were previously measured at fair value and classified as available-for-sale are now measured at fair value through profit or loss. Under IFRS 9, impairment only applies to financial assets held at amortised cost.

Summarised financial information on share investments where the Bank owned greater than or equal to 20 per cent of the investee share capital at 31 December 2010 is detailed under Note 34, “Related parties”.

³² Transfer between classes includes the reclassification of available-for-sale share investments upon an increase in the Bank's holding to between 20 and 50 per cent. The Bank designates these associate share investments at fair value through profit or loss under the venture capital exemption within IAS 28, Investments in Associates.

³³ Balances transferred or reclassified from available-for-sale (AFS) share investments and portage equities upon adoption of IFRS 9.

23. TREASURY SHARE INVESTMENTS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME

Treasury holds a strategic share investment in The Currency Exchange Fund N.V. Through this investment the Bank can access the foreign currency hedging products offered by the fund and therefore it was deemed appropriate to designate this investment to be measured at fair value through other comprehensive income.

	2010 € million	Upon transition 1 January 2009 € million
<i>Share investment designated at fair value through other comprehensive income</i>		
The Currency Exchange Fund N.V.	56	57

There was no dividend income received on this share investment during 2010.

24. INTANGIBLE ASSETS

	Computer software development costs 2010 € million	Computer software development costs 2009 € million
<i>Cost</i>		
At 1 January	138	122
Additions	11	16
At 31 December	149	138
<i>Amortisation</i>		
At 1 January	(85)	(73)
Charge	(17)	(12)
At 31 December	(102)	(85)
Net book value at 31 December	47	53

25. PROPERTY, TECHNOLOGY AND OFFICE EQUIPMENT

	Property 2010 € million	Property under construction 2010 € million	Technology and office equipment 2010 € million	Total 2010 € million	Property 2009 € million	Property under construction 2009 € million	Technology and office equipment 2009 € million	Total 2009 € million
<i>Cost</i>								
At 1 January	40	3	27	70	40	2	26	68
Additions	2	1	1	4	–	1	2	3
Transfers	1	(1)	–	–	–	–	–	–
Disposals	–	–	(1)	(1)	–	–	(1)	(1)
At 31 December	43	3	27	73	40	3	27	70
<i>Depreciation</i>								
At 1 January	(12)	–	(19)	(31)	(9)	–	(18)	(27)
Charge	(3)	–	(2)	(5)	(3)	–	(2)	(5)
Disposals	–	–	1	1	–	–	1	1
At 31 December	(15)	–	(20)	(35)	(12)	–	(19)	(31)
Net book value at 31 December	28	3	7	38	28	3	8	39

Property includes fixtures and fittings.

26. BORROWINGS

Amounts owed to credit institutions	2010 € million	2009 € million
Current	(1,911)	(2,129)

27. DEBTS EVIDENCED BY CERTIFICATES

The Bank's outstanding debts evidenced by certificates and related fair value hedging swaps are summarised below, both in the currency of the bond and the currency obtained after currency swap hedges have been taken into account.

	Adjusted principal value € million	Net currency obligations 2010 € million	Net currency obligations 2009 € million
Australian dollars	(1,392)	-	(154)
Canadian dollars	(58)	-	-
Euro	(1,859)	(5,725)	(4,126)
Japanese yen	(2,656)	(8)	(116)
Mexican peso	(112)	-	-
New Taiwan dollars	(115)	-	-
New Turkish lira	(1,080)	-	-
New Zealand dollars	(534)	-	-
Norwegian krone	(128)	-	-
Romanian leu	(67)	(4)	(4)
Russian roubles	(1,546)	(1,094)	(1,020)
South African rands	(1,294)	-	-
Sterling	(2,909)	(1,919)	(1,315)
Swedish krona	(375)	-	-
United States dollars	(8,911)	(14,286)	(10,980)
At 31 December	(23,036)	(23,036)	(17,715)

Where the swap counterparty exercises a right to terminate the hedging swap prior to legal maturity, the Bank is committed to exercise the same right with its issued bond.

Analysed between	2010 € million	2009 € million
Current	(5,674)	(5,149)
Non-current	(17,362)	(12,566)
Debts evidenced by certificates at 31 December	(23,036)	(17,715)

During the year the Bank redeemed €565 million of bonds and medium-term notes prior to maturity (2009: €258 million), generating a net gain of €24 million (2009: €13 million).

28. OTHER FINANCIAL LIABILITIES

	2010 € million	2009 € million
Fair value of derivatives designated as fair value hedges	(768)	(549)
Fair value of derivatives designated as cash flow hedges	(3)	(15)
Fair value of derivatives held for trading	(271)	(153)
Fair value of other derivatives held in relation to the Banking portfolio	(30)	(86)
Interest payable	(188)	(174)
Other	(143)	(203)
At 31 December	(1,403)	(1,180)

	2010 € million	2009 € million
<i>Analysed between</i>		
Current	(340)	(540)
Non-current	(1,063)	(640)
At 31 December	(1,403)	(1,180)

29. SUBSCRIBED CAPITAL

	2010 Number of shares	2010 Total € million	2009 Number of shares	2009 Total € million
Authorised shared capital	2,100,000	21,000	2,000,000	20,000
<i>of which</i>				
Subscriptions by members – initial capital	992,175	9,922	992,175	9,922
Subscriptions by members – first capital increase	987,175	9,872	987,175	9,872
Subscriptions by members – second capital increase	99,978	999	–	–
Subscribed capital	2,079,328	20,793	1,979,350	19,794
Unsubscribed capital	20,672	207	20,650	206
At 31 December	2,100,000	21,000	2,000,000	20,000

The Bank's capital stock is divided into paid-in shares and callable shares. Each share has a par value of €10,000. At the Bank's Annual Meeting in May 2010 the Board of Governors approved a two-step increase in the authorised capital stock of the Bank: an increase in the authorised paid-in shares of €1.0 billion and an increase in the authorised callable capital shares of €9.0 billion, for an aggregate increase in the authorised capital stock of the Bank of €10.0 billion (collectively referred to as the second capital increase). Resolution No. 126 authorised the increase in authorised capital stock by 100,000 paid-in shares, each share having a par value of €10,000, taking the authorised capital stock of the Bank to €21.0 billion. Resolution No. 128 authorised the increase in the authorised capital stock of the Bank by 900,000 callable shares, each share having a par value of €10,000, with the shares subject to redemption in accordance with the terms of Resolution No. 128. The increase in callable capital will become effective when subscriptions are received for at least 50 per cent of the newly authorised callable capital. Subscriptions are due to be received on or before 30 April 2011, but the Board of Directors may extend this date to no later than 31 December 2011.

Payment for the paid-in shares issued as part of the original authorised capital stock, and as part of the first capital increase and subscribed to by members, is made over a period of years determined in advance. Payment for the paid-in shares issued under the second capital increase was by way of a reallocation of net income previously allocated to surplus for other purposes, namely for the payment of such paid-in shares, pursuant to Article 36.1 of the Agreement and approved by Board of Governors Resolution No. 126, dated 14 May 2010. Article 6.4 of the Agreement states that payment of the amount subscribed to the callable capital is subject to call by the Bank, taking account of Articles 17 and 42 of the Agreement, only as and when required by the Bank to meet its liabilities. Article 42.1 states that in the event of the termination of the Bank's operations, the liability of all members for all uncalled subscriptions to the capital stock will continue until all claims of creditors, including all contingent claims, have been discharged.

The Agreement allows for a member to withdraw from the Bank, in which case the Bank is required to repurchase the former member's shares. No member has ever withdrawn its membership. The stability in the membership reflects the fact that the members are 61 countries and two inter-governmental organisations, and that the purpose of the Bank is to foster the transition process in politically qualifying countries from central Europe to central Asia.

Moreover, there is a financial disincentive to withdrawing membership. The upper limit of the amount of the repurchase price of the former member's shares is the amount of its paid-in capital, yet a former member remains liable for its direct obligations and its contingent liabilities to the Bank for as long as any part of the loans, share investments or guarantees contracted before it ceased to be a member are outstanding. Were a member to withdraw from the Bank, the Bank would be able to impose conditions and set dates in respect of payments for shares repurchased. If, for example, paying a former member would have adverse consequences for the Bank's financial position, the Bank could defer payment until the risk had passed, and indefinitely if appropriate. If a payment was then made to a former member, the member would be required to repay, on demand, the amount by which the repurchase price would have been reduced if the losses for which the former member remained liable had been taken into account at the time of payment.

Under the Agreement, payment for the paid-in shares of the initial capital stock subscribed to by members was made in five equal annual instalments. Of each instalment, up to 50 per cent was payable in non-negotiable, non-interest-bearing promissory notes or other obligations issued by the subscribing member and payable to the Bank at par value upon demand. Under Resolution No. 59, payment for the paid-in shares subscribed to by members under the first capital increase was made in eight equal annual instalments. Under Resolution No. 126, payment for the paid-in shares issued to members under the second capital increase was made in one instalment immediately following approval of Resolution No. 126.

A statement of capital subscriptions showing the amount of paid-in and callable shares subscribed to by each member, together with the amount of unallocated shares and votes, is set out in the following table. Under Article 29 of the Agreement, the voting rights of members that have failed to pay any part of the amounts due in respect of their capital subscription are proportionately reduced until payment is made.

Statement of capital subscriptions

	Total shares (number)	Resulting votes ³⁴ (number)	Total capital € million	Callable capital € million	Paid-in capital € million
At 31 December 2010					
Members					
Albania	2,101	1,658	21	15	6
Armenia	1,050	1,050	10	7	3
Australia	21,010	21,010	210	147	63
Austria	47,903	47,903	479	336	143
Azerbaijan	2,101	1,958	21	15	6
Belarus	4,202	4,202	42	29	13
Belgium	47,903	47,903	479	336	143
Bosnia and Herzegovina	3,550	3,550	35	25	10
Bulgaria	16,598	16,598	166	117	49
Canada	71,435	71,435	714	501	213
Croatia	7,660	7,660	77	54	23
Cyprus	2,101	2,101	21	15	6
Czech Republic	17,928	17,928	179	126	53
Denmark	25,212	25,212	252	177	75
Egypt	2,101	1,851	21	15	6
Estonia	2,101	2,101	21	15	6
European Investment Bank	63,031	63,031	630	442	188
European Union	63,031	63,031	630	442	188
Finland	26,263	26,263	263	184	79
Former Yugoslav Republic of Macedonia	1,451	1,451	15	10	5
France	178,956	178,956	1,790	1,257	533
Georgia	2,101	468	21	15	6
Germany	178,956	178,956	1,790	1,257	533
Greece	13,656	13,656	137	96	41
Hungary	16,598	16,598	166	117	49
Iceland	2,101	2,101	21	15	6
Ireland	6,303	6,303	63	44	19
Israel	13,656	13,656	137	96	41
Italy	178,956	178,956	1,790	1,257	533
Japan	178,956	178,956	1,790	1,257	533
Kazakhstan	4,832	4,832	48	34	14
Korea, Republic of	21,010	21,010	210	147	63
Kyrgyz Republic	2,101	768	21	15	6
Latvia	2,101	2,101	21	15	6
Liechtenstein	420	417	4	3	1
Lithuania	2,101	2,101	21	15	6
Luxembourg	4,202	4,202	42	29	13
Malta	210	210	2	1	1
Mexico	3,151	3,151	32	21	11
Moldova	2,101	1,404	21	15	6
Mongolia	210	210	2	1	1
Montenegro	420	420	4	3	1
Morocco	1,050	1,050	10	7	3
Netherlands	52,105	52,105	521	366	155
New Zealand	1,050	1,050	10	7	3
Norway	26,263	26,263	263	184	79
Poland	26,893	26,893	269	189	80
Portugal	8,824	8,824	88	62	26
Romania	10,085	10,085	101	71	30
Russia	84,041	84,041	840	590	250
Serbia	9,822	9,822	98	69	29
Slovak Republic	8,965	8,965	90	63	27
Slovenia	4,407	4,407	44	31	13
Spain	71,435	71,435	714	501	213
Sweden	47,903	47,903	479	336	143
Switzerland	47,903	47,903	479	336	143
Tajikistan	2,101	362	21	15	6
Turkey	24,161	24,161	242	169	73
Turkmenistan	210	149	2	1	1
Ukraine	16,808	16,568	168	118	50
United Kingdom	178,956	178,956	1,790	1,257	533
United States	210,104	210,104	2,101	1,475	626
Uzbekistan	4,412	4,044	44	31	13
Capital subscribed by members	2,079,328	2,072,418	20,793	14,596	6,197

³⁴ Voting rights are restricted for non-payment of amounts due in respect of the member's obligations in relation to paid-in shares. Total votes before restrictions amount to 2,079,328 (2009: 1,979,350).

30. RESERVES AND RETAINED EARNINGS

	2010 € million	2009 € million
Strategic reserve		
At 1 January	800	830
Transferred to paid-in capital	(800)	–
Contribution to EBRD Shareholder Special Fund	–	(30)
At 31 December	–	800
Special reserve		
At 1 January	273	250
Qualifying fees and commissions	33	23
At 31 December	306	273
Loan loss reserve		
At 1 January	778	405
Transferred from retained earnings	(25)	373
At 31 December	753	778
General reserve – other reserve		
<i>Revaluation reserve</i>		
At 31 December 2009	1,130	495
IFRS 9 reclassification of financial assets	(1,121)	–
At 1 January	9	495
Net gains arising on revaluation of share investments at fair value through other comprehensive income	(1)	–
Net gains from changes in fair value	–	369
Net losses transferred to net profit due to impairment	–	288
Net gains transferred to net profit on disposal	–	(22)
At 31 December	8	1,130
<i>Hedging reserve – cash flow hedges</i>		
At 1 January	(15)	(52)
Gains from changes in fair value recognised in equity	16	23
(Gains)/losses removed from equity and included in general and administrative expenses	(1)	14
At 31 December	–	(15)
<i>Other</i>		
At 1 January	184	180
Internal tax for the year	5	4
At 31 December	189	184
General reserve – other reserve at 31 December	197	1,299
General reserve – retained earnings		
At 31 December 2009	3,167	4,444
Effect of change in accounting policy for classification and measurement of financial assets (see “Accounting policy” section)	1,337	–
At 1 January	4,504	4,444
Qualifying fees and commissions	(33)	(23)
Transferred to paid-in capital	(199)	–
Transferred to loan loss reserve	25	(373)
Transferred from strategic reserve	–	30
Net profit/(loss) after transfers of net income approved by the Board of Governors	1,227	(911)
General reserve retained earnings at 31 December	5,524	3,167
Total reserves and retained earnings at 31 December	6,780	6,317

In 2008 the Bank created a **strategic reserve** within members’ equity to set aside a portion of net income to cover future capital requirements, other allocations and potentially to absorb any negative impact arising from adverse operational or financial developments until 2010 (the end of the CRR3 period).

The **special reserve** is maintained, in accordance with Article 16 of the Agreement, for meeting certain defined losses of the Bank. The special reserve has been established, in accordance with the Bank's financial policies, by setting aside 100 per cent of qualifying fees and commissions received by the Bank associated with loans, guarantees and underwriting the sale of securities, until such time as the Board of Directors decides that the size of the special reserve is adequate. In accordance with the Agreement, €33 million (2009: €23 million) of qualifying fees and commissions recognised in the income statement was appropriated in 2010 and set aside to the special reserve.

In 2005, the Bank created a **loan loss reserve** within members' equity, to set aside an amount of retained earnings equal to the difference between the impairment losses expected over the life of the loan portfolio and the amount recognised through the Bank's income statement on an incurred loss basis.

The **general reserve** includes the retention of internal tax paid in accordance with Article 53 of the Agreement. This requires that all Directors, Alternate Directors, officers and employees of the Bank are subject to an internal tax imposed by the Bank on salaries and emoluments paid by the Bank and which is retained for its benefit. At the end of the year internal tax amounted to €79 million (2009: €75 million).

The **hedging reserve** includes forward exchange contracts entered into by the Bank to hedge part of its estimated future sterling operating expenditure. At 31 December 2010 there were negligible unrealised mark-to-market gains on the above forward hedges (2009: €15 million). These gains remain in reserves until such time as the related hedged expenditure is incurred.

	2010 € million	2009 € million
Reserves and retained earnings		
Strategic reserve	-	800
Special reserve	306	273
Loan loss reserve	753	778
Unrealised gains	1,953	1,584
Total restricted reserves	3,012	3,435
Unrestricted general reserves	3,768	2,882
At 31 December	6,780	6,317

The Bank's reserves are used to determine, in accordance with the Agreement, what part of the Bank's net income will be allocated to surplus or other purposes and what part, if any, will be distributed to its members. For this purpose, the Bank uses unrestricted general reserves.

Article 36 of the Agreement relates to the allocation and distribution of the Bank's net income and states: "No such allocation, and no distribution, shall be made until the general reserve amounts to at least ten per cent of the authorised capital stock". This figure is currently €2.1 billion (2009: €2.0 billion).

At the 2010 Annual Meeting, the Board of Governors approved an increase of the Bank's authorised capital through €1.0 billion of paid-in shares and €9.0 billion of callable shares. In May 2010, €1.0 billion of net income (specifically €800 million from the strategic reserve and €200 million from unrestricted general reserves) was allocated as payment for the paid-in shares.

In addition, the Board of Governors approved €150 million of net income to be allocated to the EBRD Shareholder Special Fund. This is recorded below net profit in the Bank's income statement for financial reporting purposes.

31. UNDRAWN COMMITMENTS AND GUARANTEES

Analysis by instrument	2010 € million	2009 € million
Undrawn commitments		
Loans	7,217	5,766
Share investments	1,712	1,625
At 31 December	8,929	7,391
Guarantees		
Trade finance guarantees ³⁵	369	260
Other guarantees ³⁶	96	65
At 31 December	465	325
Undrawn commitments and guarantees at 31 December	9,394	7,716

32. OPERATING LEASE COMMITMENTS

The Bank leases its Headquarters building in London and some of its Resident Office buildings in its countries of operations. These are standard operating leases and include renewal options, periodic escalation clauses and are mostly non-cancellable in the normal course of business without the Bank incurring substantial penalties. The most significant lease is that for the Bank's Headquarters building. Rent payable under the terms of this lease is reviewed every five years and is based on market rates. The last review was conducted in January 2007.

Minimum future lease payments under long-term non-cancellable operating leases and payments made under such leases during the year are shown below.

Payable	2010 € million	2009 € million
Not later than one year	27	24
Later than one year and not later than five years	98	92
Later than five years	153	167
At 31 December	278	283
Expenditure incurred in the current year	23	21

The Bank has entered into sub-lease arrangements for two floors of its Headquarters building and the building previously used for the Kiev Resident Office. The total minimum future lease payments expected to be received under these sub-leases and income received during the year are shown below:

Receivable	2010 € million	2009 € million
Not later than one year	5	5
Later than one year and not later than five years	16	19
Later than five years	-	-
At 31 December	21	24
Income received in the current year	5	5

³⁵ Trade finance guarantees represent stand-by letters of credit issued in favour of confirming banks that have undertaken the payment risk of issuing banks in the Bank's countries of operations.

³⁶ Other guarantees include unfunded full or partial risk participations.

33. STAFF RETIREMENT SCHEMES

Defined benefit scheme

A qualified actuary performs a full actuarial valuation of the defined benefit scheme at least every three years using the projected unit method. For IAS 19 purposes this is rolled forward annually to 31 December. The most recent valuation date was 30 June 2009. The present value of the defined benefit obligation and current service cost was calculated using the projected unit credit method.

Amounts recognised in the statement of financial position are as follows:

	2010 € million	2009 € million
Fair value of plan assets	199	166
Present value of the defined benefit obligation	(162)	(137)
	37	29
Unrecognised actuarial losses ³⁷	28	31
Prepayment at 31 December	65	60
Movement in the prepayment (included in "Other assets"):		
At 1 January	60	31
Exchange differences	2	3
Contributions paid	17	15
Final Salary Plan payment ³⁸	-	26
Total expense as below	(14)	(15)
At 31 December	65	60
The amounts recognised in the income statement are as follows:		
Current service cost	(16)	(13)
Interest cost	(8)	(8)
Expected return on assets ³⁹	11	7
Past service credit ⁴⁰	-	1
Amortisation of actuarial loss	(1)	(2)
Total included in staff costs	(14)	(15)

Principal actuarial assumptions used:

	2010	2009
Discount rate	5.30%	5.60%
Expected return on plan assets	6.25%	6.50%
Future salary increases	4.75%	4.50%
Average remaining working life of employees	15 years	15 years

Actuarial gains and losses in excess of a corridor (10 per cent of the greater of assets or liabilities) are amortised over the remaining working life of employees.

Actual asset allocation	2010 € million	Expected return per annum	2009 € million	Expected return per annum
Equities	118	8.20%	92	8.40%
Index-linked bonds	69	3.70%	59	4.10%
Commodities	11	4.20%	9	4.40%
Derivatives	-	n/a	5	4.40%
Cash	1	0.50%	1	0.50%
Total	199	6.25%	166	6.50%

The approach used to determine the expected return on assets assumption is to set an assumption for the return on each of the main asset classes and then to weight these returns linearly according to the Plan's asset allocation. In this calculation, the return for bonds is assumed to be the same as their initial yields. At 31 December 2010, this is 4.2 per cent per annum for gilts and 3.7 per cent per annum for index-linked gilts. The expected return on equities is assumed to be 4.0 per cent above the return on gilts. It has been assumed that commodities and hedge funds have the same long-term expected return as gilts.

³⁷ These unrecognised actuarial losses represent the cumulative effect of the historical differences between the actuarial assumptions used in the production of these disclosures and the actual experience of the plan. The primary historical causes of the losses are an overall lower-than-expected investment return on plan assets, and a historical decline in the discount rate used to value the plan's liabilities.

³⁸ A one-off payment of €26 million (£24 million) was made into the Final Salary Plan at 31 March 2009.

³⁹ The actual return on assets during the year was €20 million (2009: €25 million).

⁴⁰ The past service credit reflects the change in the Plan benefits structure, due to an increase in the retirement age from age 63 to age 65 and the estimate allows for 20 per cent of active members to withdraw their full accrued benefit at age 63 and at 64.

	2010 € million	2009 € million
Changes in the present value of the defined benefit obligation		
Present value of defined benefit obligation at 1 January	137	108
Service cost	16	13
Interest cost	8	8
Effect of exchange rate movement	6	8
Actuarial loss arising due to changes in assumptions	6	9
Benefits paid	(11)	(9)
Present value of defined benefit obligation at 31 December	162	137

	2010 € million	2009 € million
Changes in the fair value of plan assets are as follows:		
Opening fair value of plan assets	166	100
Expected return	11	7
Asset gain arising during the year	9	18
Effect of exchange rate movement	7	9
Contributions paid	17	41
Benefits paid	(11)	(9)
Present value of plan assets at 31 December	199	166

	2010 € million	2009 € million	2008 € million	2007 € million	2006 € million
History of experience gains and losses					
Defined benefit obligation	162	137	108	126	136
Plan assets	199	166	100	154	153
Surplus/(deficit)	37	29	(8)	28	17
Experience gains/(losses) on plan liabilities:					
Amount	2	1	4	(4)	3
Percentage of the present value of the plan liabilities	1.2%	1.1%	3.9%	(3.6%)	1.4%
Actual return less expected return on plan assets:					
Amount	9	18	(29)	6	3
Percentage of the present value of the plan assets	4.5%	11.0%	(29.5%)	3.9%	1.3%

Defined contribution scheme

The charge recognised under the defined contribution scheme was €9 million (2009: €9 million) and is included in “General administrative expenses”.

Other long-term employee benefits

The Bank introduced a medical retirement benefit plan on 1 June 2008 to provide staff retiring from the Bank, aged 50 or over and with at least seven years service, with a lump sum benefit to help purchase medical insurance cover. The total charge for the year calculated under IAS 19 was €1 million (2009: €0.8 million).

34. RELATED PARTIES

The Bank has the following related parties:

Key management personnel

In sterling terms, salaries and other benefits paid to key management personnel in 2010 amounted to £8 million (2009: £7 million). This comprises short-term employee benefits of £7 million (2009: £6 million) and post-employment benefits of £1 million (2009: £1 million).

During 2010, consultancy contracts totalling €106,201 were awarded to close members of the family of two key management personnel with a balance of €48,490 outstanding at year-end.

Key management personnel comprise: the President and Vice Presidents; members of the Bank's Executive Committee; Managing Directors; Corporate Directors; the Treasurer; the Director, Risk Management; the Controller; the Director of Human Resources; the Head of Internal Audit; and the CCO.

Venture capital associates

The Bank has a number of venture capital associates that it accounts for at fair value through profit or loss. At 31 December 2010, according to unaudited management information or the most recently audited financial statements from the investee companies, these venture capital associates had total assets of approximately €66.0 billion (2009: €36.1 billion) and total liabilities of approximately €44.6 billion (2009: €27.3 billion). For the year ended 31 December 2010, these associates had revenue of €19.9 billion (2009: €6.8 billion) and made a net profit of approximately €2.1 billion (2009: €0.4 billion).

In addition, the Bank has provided €128 million (2009: €108 million) of financing to these companies on which it received €4 million (2009: €4 million) of interest income during the year.

Special Funds

Special Funds are established in accordance with Article 18 of the Agreement Establishing the Bank and are administered under the terms of rules and regulations for each such Special Fund. At 31 December 2010 the Bank administered 15 Special Funds comprising 13 Investment Special Funds, eight of which also contain a technical cooperation component, and two Technical Cooperation Special Funds.

The Bank acts as manager and administrator of the Special Funds. In its capacity as manager and administrator, the Bank receives management and cost recovery fees, which in 2010 amounted to €2 million (2009: €0.3 million). Additionally, following approval by the Bank's members, the Bank contributed €150 million (2009: €30 million) to the EBRD Shareholder Special Fund as a re-allocation of net income previously allocated to surplus.

The Bank pays for guarantees from certain Special Funds in respect of specific exposures arising in its loan and trade finance portfolios. During 2010, the Bank paid guarantee fees of €0.3 million (2009: €0.3 million). At 31 December 2010 the Bank recognised a receivable of €4 million (2009: €4 million) to reflect a potential recovery in relation to an impaired trade finance investment.

Summary of Special Funds

The financial statements of each Special Fund are approved separately by the Board of Governors. A brief description of each Special Fund is summarised below and a summary of the contributions pledged by each donor country is provided overleaf.

Audit fees payable to the Bank's auditors for the 2010 audits of the 15 Special Funds totalled €98,000 (2009: €83,000).

The objectives of the Special Funds are as follows:

The Balkan Region Special Fund	To assist the reconstruction of Albania, Bosnia and Herzegovina, Bulgaria, Croatia, FYR Macedonia, Montenegro, Romania and Serbia.
The Baltic Investment Special Fund	To promote private sector development through support for small and medium-sized enterprises in Estonia, Latvia and Lithuania.
The Central Asia Risk Sharing Special Fund	To provide a risk-sharing facility for SME credit lines, microfinance programmes, the Direct Investment Facility and the Trade Facilitation Programme in the Kyrgyz Republic, Tajikistan, Turkmenistan and Uzbekistan.
The EBRD CIF Special Fund	To provide resources in support of activities that promote low carbon technologies with significant potential for long-term greenhouse gas emissions savings and other climate change activities.
The EBRD Shareholder Special Fund	To assist the Bank to achieve its mandate of promoting transition towards open market-oriented economies by preparing the way for future Bank-financed projects and improving the investment climate in the Bank's countries of operations.
The EBRD SME Special Fund	To assist the development of small and medium-sized enterprises (SMEs) in Albania, Armenia, Azerbaijan, Bosnia and Herzegovina, Bulgaria, Croatia, FYR Macedonia, Georgia, Kazakhstan, Kyrgyz Republic, Moldova, Montenegro, Romania, Serbia, Tajikistan, Turkmenistan, Ukraine and Uzbekistan.
The EBRD Technical Cooperation Special Fund	To serve as a facility for financing technical cooperation projects in countries of operations of the Bank.
The Financial Intermediary Investment Special Fund	To support financial intermediaries in the countries of operations of the Bank.
The Italian Investment Special Fund	To assist the modernisation, restructuring, expansion and development of small and medium-sized enterprises in certain countries of operations of the Bank.
The Municipal Finance Facility Special Fund	To alleviate the financing problems of municipalities and their utility companies for small infrastructure investments in Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovak Republic and Slovenia.
The RDI Special Fund	To provide a long-term contribution to sustainable socio-economic development across Azerbaijan and Georgia.
The RMC Facility Special Fund	To improve access to finance for micro and small enterprises in Romania through the Romania Micro Credit (RMC) Facility.
The Russia Small Business Investment Special Fund and The Russia Small Business Technical Cooperation Special Fund	To assist the development of small businesses in the private sector in Russia.
The SME Finance Facility Special Fund	To alleviate the financing problems of small and medium-sized enterprises in Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovak Republic and Slovenia.

	Central				Financial				Municipal		Russia		Russia		Russia	
	Balkan Region Special Fund	Baltic Investment Special Fund	Asia Risk Sharing Special Fund	EBRD CIF Special Fund	EBRD Shareholder Special Fund	EBRD SME Special Fund	EBRD Intermediary Investment Special Fund	Italian Investment Special Fund	Finance Facility Special Fund	RDI Special Fund	RMC Facility Special Fund	Business Investment Special Fund	SME Finance Facility Special Fund	Technical Cooperation Special Fund	Small Business Technical Cooperation Special Fund	EBRD Technical Cooperation Special Fund
Austria	276	-	-	-	-	-	-	-	-	-	-	-	-	-	-	276
British Petroleum (BP)	-	-	-	-	-	-	-	-	-	3,920	-	-	-	-	-	3,920
Canada	1,472	-	-	-	-	-	-	-	-	-	-	2,268	-	4,309	-	8,049
Clean Technology Fund	-	-	-	53,555	-	-	-	-	-	-	-	-	-	-	-	53,555
Denmark	750	571	-	-	-	-	-	-	-	-	-	-	-	-	-	1,321
EBRD Shareholders	-	-	-	-	295,000	-	-	-	-	-	-	-	-	-	-	295,000
European Union (EU)	-	-	-	-	-	-	-	-	33,000	-	-	-	196,673	-	-	229,673
Finland	-	551	-	-	-	-	-	-	-	-	-	-	-	-	-	551
France	-	-	-	-	-	-	-	-	-	-	-	6,725	-	4,980	-	11,705
Germany	-	-	2,389	-	-	-	-	-	-	-	-	8,476	-	3,025	-	13,890
Iceland	-	27	-	-	-	-	-	-	-	-	-	-	-	-	-	27
Italy	-	-	-	-	-	-	-	21,024	-	-	-	7,689	-	1,360	-	30,073
Japan	-	-	-	-	-	-	-	-	-	-	-	19,381	-	3,295	-	22,676
Netherlands	-	-	-	-	-	-	9,500	-	-	-	-	-	-	-	-	9,500
Norway	1,568	494	-	-	-	-	-	-	-	-	-	-	-	-	-	2,062
Romania/EU	-	-	-	-	-	-	-	-	-	-	18,020	-	-	-	-	18,020
Russia Small Business Investment Special Fund	-	-	-	-	-	-	-	-	-	-	-	-	-	3,392	-	3,392
Strategic Climate Fund	-	-	-	543	-	-	-	-	-	-	-	-	-	-	-	543
Sweden	-	1,007	-	-	-	-	-	-	-	-	-	-	-	-	-	1,007
Switzerland	4,218	-	6,199	-	-	-	-	-	-	-	-	2,236	-	1,244	-	13,897
Taipei China	1,495	-	-	-	-	-	19,745	-	-	-	-	-	-	-	-	21,240
United Kingdom	-	-	-	-	-	-	-	-	-	-	-	-	-	12,824	247	13,071
United States of America	-	-	-	-	-	37,139	847	-	-	-	-	6,039	-	29,695	-	73,720
Total at 31 December 2010	9,779	2,650	8,588	54,098	295,000	37,139	30,092	21,024	33,000	3,920	18,020	52,814	196,673	64,124	247	827,168

35. OTHER FUND AGREEMENTS

In addition to the Bank's ordinary operations and the Special Funds programme, the Bank administers numerous bilateral and multilateral contribution agreements to provide technical assistance and investment support grants in its countries of operations. These grants focus primarily on project preparation, project implementation (including goods and works), advisory services and training. The resources provided through these contribution agreements are held separately from the ordinary capital resources of the Bank and are subject to external audit.

From its inception until 31 December 2010, the Bank has administered 205 technical cooperation fund agreements (2009: 184) amounting to an aggregate of €1.7 billion (2009: €1.3 billion). Of this pledged amount, funds received at 31 December 2010 totalled €1.5 billion (2009: €1.2 billion). The total uncommitted balance of the funds at 31 December 2010 was €562 million (2009: €224 million). In addition, the Bank has administered 92 project-specific technical cooperation agreements (2009: 90) totalling €61 million (2009: €59 million).

For the specific purpose of co-financing EBRD projects, the Bank has also administered 30 investment cooperation fund agreements (2009: 29) totalling €258 million (2009: €250 million), and two EU Pre-accession Preparation Funds (2009: two) totalling €35 million (2009: €35 million).

Following a proposal by the G-7 countries for a multilateral programme of action to improve safety in nuclear power plants in the countries of operations, the Nuclear Safety Account (NSA) was established by the Bank in March 1993. The NSA funds are in the form of grants and are used for funding safety improvement measures. At 31 December 2010, 17 contributors (2009: 17) had made pledges totalling €322 million (2009: €320 million), using the fixed exchange rates defined in the rules of the NSA.

At their Denver Summit in June 1997, the G-7 countries and the European Union endorsed the setting up of the Chernobyl Shelter Fund (CSF). The CSF was established on 7 November 1997, when the rules of the CSF were approved by the Board of Directors. It became operational on 8 December 1997, when the required eight contributors had entered into contribution agreements with the Bank. The objective of the CSF is to assist Ukraine in transforming the existing Chernobyl sarcophagus into a safe and environmentally stable system. At 31 December 2010, 24 contributors (2009: 24) had made pledges totalling €841 million (2009: €807 million) using the fixed exchange rates defined in the rules of the CSF.

In 1999, in pursuit of their policy to accede to the European Union, Lithuania, Bulgaria and the Slovak Republic gave firm commitments to close and decommission their nuclear power plant units with RBMK and VVER 440/230 reactors by certain dates. In response to this, the European Commission announced its intention to support the decommissioning of these reactors with substantial grants over a period of eight to 10 years, and invited the Bank to administer three International Decommissioning Support Funds (IDSFs). On 12 June 2000, the Bank's Board of Directors approved the rules of the Ignalina, Kozloduy and Bohunice IDSFs and the role of the Bank as their administrator. The funds will finance selective projects to help carry out the first phase of decommissioning the designated reactors. They will also finance measures to facilitate the necessary restructuring, upgrading and modernisation of the energy production, transmission and distribution sectors and improvements in energy efficiency that are a consequence of the closure decisions. At 31 December 2010, 16 contributors (2009: 16) had made pledges to the Ignalina IDSF totalling €697 million (2009: €677 million); 11 contributors (2009: 11) had made pledges to the Kozloduy IDSF totalling €658 million (2009: €583 million); and nine contributors (2009: nine) had made pledges to the Bohunice IDSF totalling €435 million (2009: €375 million), using the fixed exchange rates defined in the rules of the funds.

In 2001, the Nordic Investment Bank hosted a meeting with participants from Belgium, Finland, Sweden, the European Commission and international financial institutions with activities in the Northern Dimension Area (NDA). At this meeting, participants agreed to establish the Northern Dimension Environmental Partnership (NDEP) to strengthen and coordinate financing of important environmental projects with cross-border effects in the NDA. On 11 December 2001 the Bank's Board of Directors approved the rules of the NDEP Support Fund and the role of the Bank as fund manager. At 31 December 2010, 12 contributors (2009: 12) had made pledges totalling €312 million (2009: €277 million).

Audit fees payable to the Bank's auditors for the 2010 audits of the technical cooperation and nuclear safety funds totalled €0.4 million (2009: €0.4 million). No other fees were earned by the Bank's auditors in respect of the technical cooperation funds during 2010. In 2009, the Bank's auditors on a global basis earned €0.2 million in respect of due diligence and general business consultancy services funded by the technical cooperation funds. This represented 0.3 per cent of the total spend in 2009 by the technical cooperation funds on services from consultancy providers in support of the Bank's investments in the countries of operations. These consultancy contracts are awarded in accordance with the Bank's standard procurement rules.

36. POST-STATEMENT OF FINANCIAL POSITION EVENTS

Movements in the financial markets in 2011 have resulted in an increase in the fair value of the Bank's equity portfolio due to movements in listed equity prices and foreign exchange rates. At 14 February 2011 the fair value of the share investment portfolio, net of equity derivatives, was €205 million higher than at 31 December 2010. On 15 February 2011 the Board of Directors submitted the audited financial statements of the Bank to the Board of Governors for approval at the 2011 Annual Meeting of the EBRD Board of Governors.

Responsibility for external financial reporting

MANAGEMENT'S RESPONSIBILITY

Management's report regarding the effectiveness of internal controls over external financial reporting

The management of the European Bank for Reconstruction and Development ("the Bank") is responsible for the preparation, integrity, and fair presentation of its published financial statements and all other information presented in this *Financial Report*. The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board.

The financial statements have been audited by an independent accounting firm, which has been given unrestricted access to all financial records and related data, including minutes of all meetings of the Board of Directors and committees of the Board. Management believes that all representations made to the external auditors during their audit were valid and appropriate. The external auditors' report accompanies the audited financial statements.

Management is responsible for establishing and maintaining effective internal control over external financial reporting for financial presentations in conformity with IFRS. The system of internal control contains monitoring mechanisms, and actions are taken to correct deficiencies identified. Management believes that internal controls for external financial reporting – which are subject to scrutiny and testing by management and internal audit, and are revised as considered necessary – support the integrity and reliability of the financial statements.


There are inherent limitations in the effectiveness of any system of internal control, including the possibility of human error and the circumvention of overriding controls. Accordingly, even an effective internal control system can provide only reasonable assurance with respect to financial statements. Furthermore, the effectiveness of an internal control system can change with circumstances.

The Bank's Board of Directors has appointed an Audit Committee, which assists the Board in its responsibility to ensure the soundness of the Bank's accounting practices and the effective implementation of the internal controls that management has established relating to finance and accounting matters. The Audit Committee is comprised entirely of members of the Board of Directors. The Audit Committee meets periodically with management in order to review and monitor the financial, accounting and auditing procedures of the Bank and related financial reports. The external auditors and the internal auditors regularly meet with the Audit Committee, with and without other members of management being present, to discuss the adequacy of internal controls over financial reporting and any other matters that they believe should be brought to the attention of the Audit Committee.

The Bank has assessed its internal controls over external financial reporting for 2010. Management's assessment includes the Special Funds and other fund agreements referred to in pages 83-85 of the *Financial Report 2010*, and the retirement plans. However, the nature of the assessment is restricted to the controls over the reporting and disclosure of these funds, rather than the operational, accounting and administration controls in place for each fund.

The Bank's assessment was based on the criteria for effective internal controls over financial reporting described in the "Internal Control – Integrated Framework" issued by the Committee of Sponsoring Organisations of the Treadway Commission. During the current year two incidents of alleged fraud and corruption were detected by management. Management have investigated both incidents and are satisfied that there is no impact to the financial statements. Based upon this assessment, and giving consideration to management's investigation regarding the two incidents of alleged fraud and corruption, management asserts that, at 31 December 2010, the Bank maintained effective internal controls over its financial reporting as contained in the *Financial Report 2010*.

The Bank's external auditors have provided an audit opinion on the fairness of the financial statements presented within the *Financial Report 2010*. In addition, they have issued an attestation report on management's assessment of the Bank's internal control over financial reporting, as set out on page 87.



Thomas Mirow
President



Manfred Schepers
Vice President, Finance and Chief Financial Officer

European Bank for Reconstruction and Development
London
15 February 2011

REPORT OF THE INDEPENDENT AUDITORS

To the Governors of the European Bank for Reconstruction and Development

We have examined management's assessment that the European Bank for Reconstruction and Development ("the Bank") maintained effective internal controls over financial reporting as contained in the Bank's *Financial Report 2010*, based on the criteria for effective internal controls over financial reporting described in the "Internal Control – Integrated Framework" issued by the Committee of Sponsoring Organisations of the Treadway Commission. Management is responsible for maintaining effective internal controls over financial reporting and for the assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assertion over the effectiveness of the Bank's internal control over financial reporting, based on our examination.

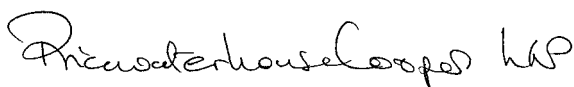
We conducted our examination in accordance with the International Standard on Assurance Engagements (ISAE) 3000. Our examination included obtaining an understanding of internal control over financial reporting, evaluating management's assessment and performing such other procedures as we considered necessary in the circumstances. We believe that our work provides a reasonable basis for our opinion.

A bank's internal controls over financial reporting are designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A bank's internal controls over financial reporting include those policies and procedures that: (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the bank; (2) provide reasonable assurance that the transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the bank are being made only in accordance with the authorisation of the bank's management; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorised acquisition, use, or disposition of the bank's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

In our opinion, management's assertion that the Bank maintained effective internal control over financial reporting, included within the Responsibility for external financial section of the Bank's *Financial Report 2010*, is fairly stated, in all material respects, based on the criteria for effective internal controls over financial reporting described in the "Internal Control – Integrated Framework" issued by the Committee of Sponsoring Organisations of the Treadway Commission.

This report, including the opinion, has been prepared for, and only for, the Board of Governors as a body in connection with management's attestation for maintaining effective internal controls over financial reporting and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come, save where expressly agreed by our prior consent in writing.



PricewaterhouseCoopers LLP

Chartered Accountants

London

15 February 2011

Independent auditors' report to the Governors of the European Bank for Reconstruction and Development

Report on the financial statements

We have audited the financial statements of the European Bank for Reconstruction and Development ("the Bank") which comprise the statement of financial position as at 31 December 2010 and the income statement, the statement of comprehensive income, the statement of changes in members' equity and the statement of cash flows for the year then ended, the accounting policies, the risk management section and notes to the financial statements ("financial statements").

President's responsibility for the financial statements

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

Auditors' responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the 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 the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors 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. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Bank at 31 December 2010 and its financial performance and cash flows for the year then ended in accordance with the International Financial Reporting Standards issued by the International Accounting Standards Board.

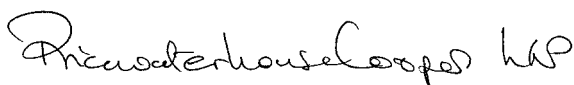
Other reporting responsibilities

We also report to you if, in our opinion, the financial results section of the *Financial Report 2010* is not consistent with the financial statements, if the Bank has not kept proper accounting records, or if we have not received all the information and explanations we require for our audit.

We read the other information contained in the *Financial Report 2010* and consider whether it is consistent with the financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. The other information comprises only the highlights, financial results, additional reporting and disclosures and Summary of Special Funds. Our responsibilities do not extend to any other information.

Other matters

This report, including the opinion, has been prepared for, and only for, the Board of Governors as a body in accordance with Article 24 of the Agreement Establishing the Bank dated 29 May 1990, and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come, save where expressly agreed by our prior consent in writing.



PricewaterhouseCoopers LLP

Chartered Accountants

London

15 February 2011

Controller's Office

Glenn Bruce
Terry Cullen
Wendy Kang
Nigel Kerby

Editorial Production

Tara Hawes
Lucy Plaskett
Jane Ross

Design and Print Management

Alan Bates Design
Daniel Kelly

European Bank for Reconstruction and Development

One Exchange Square
London EC2A 2JN
United Kingdom

Switchboard/central contact

Tel: +44 20 7338 6000
Fax: +44 20 7338 6100
SWIFT: EBRDGB2L

Information requests

For information requests and general enquiries, please use the information request form at www.ebrd.com/inforequest

Project enquiries

Tel: +44 20 7338 7168
Fax: +44 20 7338 7380
Email: projectenquiries@ebrd.com

EBRD publications

Tel: +44 20 7338 7553
Fax: +44 20 7338 6102
Email: pubsdesk@ebrd.com

Web site

www.ebrd.com

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