



2009

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ANNUAL REPORT & ACCOUNTS

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EIIB is committed to excellence in the delivery of Sharia'a compliant investment banking products and services.

## In the name of Allah, the Most Gracious, the Most Merciful To the shareholders of the European Islamic Investment Bank plc

I present to our shareholders the European Islamic Investment Bank plc's ('EIIIB' or 'Bank') results for 2009.

2009 has been another extraordinary year for global financial markets with capitalisation and liquidity concerns affecting a large number of financial institutions. Liquidity, increased provisioning levels, exposure to the Real Estate sector and low real returns on Money Market activities were themes which characterised the Islamic financial markets during this period.

The Board of EIIIB recognised at an early stage that 2009 would be a challenging year and I am pleased to report that the Bank has remained highly liquid; (+361% vs. the FSA minimum of -5%). This coupled with the strong capital position (£132.9m vs. the FSA minimum of £13.6m) has meant that the Bank has been better positioned than most to weather the storm.

The overall result for the year of a loss of £22.2m, whilst disappointing, is broadly in line with the result at the end of the first half of the year. Operating Profit on continued operations before tax, fair value losses, impairments and oil & gas activity declined from £4.3m in 2008, to a loss of £4.0m in 2009. The move from profit to loss was primarily driven by the unprecedented decline in market yields, indeed at the operating level, core Operating Expenses (excluding fair value adjustments, impairment provisions and operating expenses on oil and gas activities) remained static at £7.8m between 2008 and 2009.

Islamic Capital Markets experienced a significant recovery during the second half of 2009, after a subdued first half. A number of high quality entities, e.g. Petronas, GE Capital Corp, Islamic Development Bank, Tourism Development and Investment Company and International Finance Corporation successfully issued Sukuk during this period, proving that investors retained an appetite for well rated issuers. Unfortunately events in Dubai towards the end of the year had a materially negative impact on market sentiment, causing the recovery to largely stall.

The Bank continues to actively manage its exposures to Ahmad Hamad Algosabi and Brothers Company and Saad Golden Belt 1 Sukuk. Events at these enterprises have been the subject of much debate and speculation in the media and after careful consideration the Directors' have concluded that the timeframe, and ultimate recovery of these amounts are highly uncertain and have therefore decided to increase provisions against these exposures up to £13.4m.

The Bank's Private Equity capability has continued its development during 2009, reflecting the surge of potential investment opportunities which have arisen as the Bank has become recognised as an investor of choice. The Board has maintained its careful and prudent approach to the valuation of Private Equity investments, as we believe that this is the only way to develop a credible long term track record of investment performance. With this in mind, the Board has decided to provide £5.1m against the investments in DiamondCorp Plc and TriTech.

During the last quarter of 2009, the Bank undertook a capital reduction and tender offer. The transaction was conducted to provide some liquidity for smaller shareholders who wished to realise some or all of their investment in the Bank. The capital reduction and tender were successfully concluded in December 2009.

As noted in my Interim Statement, during the third quarter of 2009, the Bank received a number of approaches from third parties who were interested in a business combination with EIIB. The Board determined that the approaches did not make strategic sense, nor did they fairly reflect the value of EIIB, hence the discussions were terminated.

On 30 December 2009 the Pan-European Islamic Real Estate Fund was sold to ED Limited, a Cayman Islands registered company. The disposal of this entity effectively concluded the disposal of the property portfolio originally acquired in 2007 by its subsidiary The House Limited, and hence, the loss (£7.1m) accounted for in the Interim income statement was reversed in the second half of 2009.

As I noted in my Interim Statement, Mr. John Weguelin, decided to stand down as CEO of EIIB in August 2009. An extensive search process is currently underway to find a replacement CEO; whilst this process is taking longer than the Board would like, it is obviously vital to ensure that the right person is found for this key role. In the meantime, on behalf of the Board, I would like to take this opportunity to thank Mr Keith McLeod for

his continuing diligent and professional stewardship of the Bank during this transitional period.

The strategic review of the Bank's activities referred to in my interim statement has made substantial progress. The new CEO will be charged with refining and concluding the Bank's new strategic development, as well as delivering the strategic vision.

I am excited about the Bank's prospects as it moves into this next phase of development. There will be many fresh challenges ahead, but I am confident that EIIB will start to deliver the building blocks required to construct a long term profitable future.



Adnan Ahmed Yousif  
*Chairman*

### Introduction

The Directors present the Operating and Financial Review for 2009. Having followed the framework set out in the Accounting Standards Board's Reporting Statement: Operating and Financial Review as a guide to best practice, the Directors believe they have discharged their responsibilities under Section 417 of the Companies Act 2006 to provide a balanced and comprehensive review of the development and performance of the business.

### EIIB'S objectives and market environment

EIIB was the first independent Sharia'a compliant investment bank to be authorised by the Financial Services Authority (FSA). The Bank received its authorisation on 8 March 2006 and is listed in the UK on the Alternative Investment Market within the London Stock Exchange.

The Bank was established to bridge the gap between the financial markets of the Islamic world and those of Western and OECD territories. It delivers products and services across asset classes to the Islamic wholesale, institutional, and high net worth individual markets. The Bank's competitive positioning is significantly enhanced by its base in the pre-eminent global financial centre, London.

The key principles of Islamic banking are derived from the Quran and are based on the avoidance of:

- Interest
- Uncertainty
- Speculation
- Unjust enrichment or unfair exploitation

The Bank's Sharia'a Supervisory Board, comprising eminent Islamic scholars, is tasked with ensuring that all products are structured to reflect these principles.

### Business objectives

The current operations of the Bank are organised into two business units:

#### Treasury and capital markets

EIIB's Treasury engages in foreign exchange spot and the Islamic equivalent of forward foreign exchange markets and promotes liquidity in the Islamic money markets. The unit manages the short and medium term liquidity profile of the Bank within the guidelines laid down by

the FSA and the Bank's Asset and Liability Committee. In addition to being involved in Islamic interbank commodity murabaha and wakala money markets, it seeks to build a sustainable base of third party deposits by establishing direct relationships and structured investment products.

The Capital Markets unit's remit covers a range of activities including, but not limited to, term financing, Sukuk and structured trade finance. It is involved in all aspects of the product value chain, including origination, structuring, underwriting and distribution. The Bank invests in mandated financing issues and develops and maintains an active secondary market in such issues.

#### Private equity and corporate advisory

EIIB's Private Equity and Corporate Advisory Team ('PECA') operates a private equity investment business and provides advisory services to the Bank's clients. PECA sources opportunities to invest in both private and stock exchange listed companies and invests in businesses that meet the criteria set by the Bank's Board Executive Committee. PECA's investment remit is to source transactions primarily from outside of the Gulf Co-operation Council countries and, whilst that remit is global, PECA focuses on investment opportunities within Europe, the Middle East, USA and Africa.

Investee companies are sought that are revenue producing, recession resistant and have good prospects of generating significant upside within a target period of two to four years.

### Business strategy and results

2009 continued to be exceptionally challenging for all financial institutions. The overriding themes of depressed asset prices and lack of confidence resulted in very low transaction volumes in the Islamic capital markets. Low profit rates in the Sukuk, murabaha and wakala markets reflected the low global base rate environment.

EIIB's results at the consolidated level reflect a loss of £22.2m after tax. The loss reflects the subdued operating environment, and fair value and impairment provisions against two Capital Markets and two Private Equity assets.

EIIB makes term financing facilities available under a number of Sharia'a compliant structures. Prior to committing any financing, EIIB undertakes rigorous

credit and risk assessment of the obligor. Capital Markets funding made available to Ahmed Hamad Algosabi and Brothers Company and Saad Golden Belt 1 Sukuk Company have defaulted during the year and EIIB has made provisions of £13.4m against these.

The Private Equity and Corporate Advisory business acquired its second asset, an interest in a joint venture oil and gas exploration activity during 2009. The division's first acquisition, DiamondCorp Plc, a diamond production company operating in South Africa, has suffered severe financial difficulties during the year. The Oil & gas venture is still in the exploration stage and its success is yet to be determined. In line with Boards' cautious approach on asset valuation, £5.1m is recognised as fair value deterioration and impairment against the two investments made.

EIIB held an interest in a portfolio of UK commercial property through a shareholding in the Pan-European Islamic Real Estate Fund ("PEIREF"). The portfolio was owned by The House Limited ("THL"), a subsidiary of PEIREF. Following a breach of a covenant by THL at the end of 2008 the third-party financial institution that provided senior funding to THL, exercised their security and appointed a receiver to take over the property portfolio. In December 2009 EIIB sold its interest in PEIREF. EIIB's investment in PEIREF was fully written-off by the end of 2008 and hence the 2009 annual financial statements are not impacted by the sale (the net liability position of PEIREF that was reflected in the consolidated interim financial statements -June 2009- has reversed following the disposal).

## People

A significant differentiating factor for our business has been our ability to attract quality staff from the London market. The Directors believe that the Bank has a competitive remuneration structure, which enables EIIB to retain and attract staff of the highest calibre.

## Operational

The Bank has built an operational infrastructure that is robust and scalable. The Directors are confident that the controls around these systems and processes are effective in protecting and safeguarding the Bank's assets. EIIB's Internal Audit department, under the direction of the Board's Audit Committee, is responsible for working with management to identify and quantify

risk, provide independent appraisals of systems of internal control, add value to business initiatives and support development of a sound control culture throughout the Bank.

## Risks

EIIB is exposed to market risk in relation to its proprietary investments, counterparty risk from transactions with third parties, particularly money market transactions, liquidity risk from liquidity mismatches and operational risk.

The Bank's measured approach to risk is documented in the risk policy. Under this policy risk is monitored on a daily basis. Further details are reported in Note 34.

## Key performance indicators

The Board are of the view that management should build the business while tracking performance against indicators such as return on equity ('ROE'), staff turnover and efficiency. As business activities further develop, the Bank will benchmark these key performance indicators ('KPI's') against international Islamic banking institutions. The Bank does not consider it meaningful at this point to disclose numerical targets and performance indicators.

## Non-Executive Directors

### **Adnan Ahmed Yousif\***

Chairman of the Board of EIIB. President and Chief Executive of the Albaraka Banking Group (ABG) and Chairman of the Union of Arab Banks. He was Chief Executive Officer and Board Member of the Bahrain Islamic Bank from 2002 to 2004. He is also Chairman of Albaraka Turk Participation Bank, Banque Al Baraka D'Algerie, Albaraka Bank South Africa, Albaraka Lebanon, Jordan Islamic Bank, Egyptian Saudi Finance Bank and Vice Chairman of Albaraka Islamic Bank. He held various senior positions at Arab Banking Corporation (ABC) over a 20 year period, including: Board Member of the parent company and Member of the Audit Committee; the Executive Chairman of ABC Services & Investment Company and ABC Islamic Bank; Senior Vice President and Head of the Arab World Division; and Head of Global Marketing & Financial Institutions Division. He started his banking career with American Express Bank and his overall international banking experience spans more than 34 years. He was awarded the prestigious Islamic Banker of the Year award for 2004 and 2009.

### **Shabir Randeree\*** (2, 3, 4)

Deputy Chairman of the Board of EIIB and Chairman of the Remuneration Committee. He is Chairman of DCD London & Mutual, a family investment office and holds a number of other directorships, including that of Deputy Chairman of Albaraka Bank, South Africa. He holds a BA(Hons) in Accounting and Finance and a MBA.

### **Salman Abbasi\*** (3)

Chairman of the Nomination Committee. Joined Investcorp Bahrain as a member of the Management Committee in early 1988 and was General Manager of Investcorp Bahrain from then until 2004 when he retired. He was associated with Chase Manhattan Bank from 1967 serving for 20 years in a variety of positions both at the head office in New York and overseas. In his last position prior to joining Investcorp he was Vice President and Chief Executive responsible for managing all Chase business in Africa and the Middle East. He also served concurrently as a Director on the boards of Saudi Investment Bank and Chase Bank Cameroon. His total banking career exceeds 40 years.

### **Yusef Abu Khadra\*** (1, 2, 4)

Formerly a Member of the Management Committee of Investcorp Bahrain and latterly an Executive Director of Investcorp Securities in London until his retirement in 2005. He has also served with Morgan Stanley in London and New York, and has held a number of positions in financial services based in the Middle East and Switzerland. His banking experience spans nearly 36 years. Currently he is trustee of the American University of Beirut and a director of the Council of British Arab Understanding. He holds a Masters Degree in Finance from Michigan State University.

### **Zaher Al-Ajjawi** (1)

Director Financial Investments at Premier Group Bahrain. Previously he was Vice President, Real Estate Investment Banking at Morgan Stanley Dubai; Executive Director, Real Estate Unit at Gulf Finance House; and Supervising Senior Auditor at KPMG. Mr. Al-Ajjawi holds a Bachelor of Accounts from Bahrain University and is a CPA.

**Mohammed Al Sarhan\*** (3, 4)

Senior Independent Director of EIIB. Vice President and Chief Operating Officer of Al Faisaliah Group, Kingdom of Saudi Arabia since 2001. Previously he was Managing Director of Al Safi Danone Co. and Vice President of Samarec. He is Vice Chairman of the National Shipping Company of Saudi Arabia; Board Member of Saudi Arabian Public Transport Company; Board Member of Al Safi Danone Co.; Board Member of Saudi Fresh Dairy Board and President of the Al Safi Club for Friends of the Environment. Mr. Al Sarhan holds a B.Sc (Mathematics) from Oregon State University, USA.

**Aabed Alzeera\*** (2, 4)

Chairman of the Board Executive Committee. A prominent Bahraini banker, he has almost 30 years of international banking experience with major financial institutions in the Kingdom of Bahrain and the United Arab Emirates, including American Express Banking Corporation, Arab Banking Corporation (ABC), Standard Chartered Bank, and First Islamic Investment Bank (now Arcapita). Mr. Al Zeera was also instrumental in setting up ABC's Representative Office in Abu Dhabi in 1996, where he served as Vice President and Chief Representative. He is currently a Board Member and the Chief Executive Officer of International Investment Bank, an Islamic investment bank established in the Kingdom of Bahrain, in which he was a founding shareholder and the key promoter as well.

**Subhi Benkhadra\*** (1, 2, 4)

Chief Executive Officer of Esterad Investment Company, Bahrain. He was previously Chief Executive Officer and Managing Director of Investment Trust Limited; Deputy Managing Director of Primecorp Investment Management Limited and Head of Arab Capital Markets at United Bank of Kuwait. He holds a B.Sc (Engineering) from the University of Bath, UK and an MBA from City University Business School, UK.

**George Morton\*** (1, 4)

Chairman of the Audit Committee. He has spent over 40 years in government service and international banking, principally in East Asia and the Arabian Gulf, including senior positions with Arab Banking Corporation, National Bank of Bahrain and Gulf International Bank. He holds an MA in East Asian History from the University of Toronto and is also currently a Lay Member of the Governing Council of the University of Bristol.

## Executive Director

**Keith McLeod**

Acting Chief Executive Officer and Finance Director of EIIB. He started his career at, and qualified as a chartered accountant with, Price Waterhouse. Before joining EIIB, he was Executive Director, Head of Fund Services and Logistics Reporting at UBS Global Asset Management. He has held senior positions at Schroders, Credit Suisse First Boston, Morgan Stanley and HSBC. He holds a B.Sc (Economics) from the London School of Economics, UK.

(1) Member of the Audit Committee

(2) Member of the Remuneration Committee

(3) Member of the Nomination Committee

(4) Member of the Board Executive Committee

\* Independent Director

The Directors of European Islamic Investment Bank plc have pleasure in presenting their annual report, together with the audited financial statements, for the year ended 31 December 2009.

## PRINCIPAL ACTIVITIES

European Islamic Investment Bank plc was incorporated in the United Kingdom on 11 January 2005, and commenced full banking operations in April 2006. The Bank is the first independent Sharia'a compliant investment bank in the United Kingdom to be regulated by the FSA. The Bank services a market for Sharia'a compliant investment banking services internationally.

## FINANCIAL RESULTS

The financial statements for the reporting year ended 31 December 2009 are shown on pages 16 to 65. The loss for the year after taxation amounts to £22.2m (2008: loss £14.8m).

## DIVIDEND

The Bank has no plans to declare a dividend.

## DIRECTORS

The Directors serving at the date of this report and throughout the year are shown on pages 6 and 7.

John Weguelin, a director and the Bank's Chief Executive Officer, resigned on 21 August 2009. The Finance Director, Keith McLeod was appointed Acting Chief Executive Officer from 21 August 2009.

## DIRECTORS' INTERESTS

The Directors who held office at the end of the financial year had the following beneficial interests in the ordinary shares of the Bank according to the register of Directors' interests. The table shows the number of shares held and as a percentage of total shares in issue at that time:

	Class of share	Number of shares	Interest at end of year	Number of shares	Interest at start of year
Adnan Ahmed Yousif	Ordinary 1p	2,000,000	0.11%	2,000,000	0.11%
George Morton	Ordinary 1p	1,000,000	0.06%	1,000,000	0.05%
Shabir Randeree	Ordinary 1p	1,524,783	0.09%	1,524,783	0.08%
Mohammed Al Sarhan	Ordinary 1p	3,049,567	0.17%	3,049,567	0.17%

None of the other Directors who held office at the end of the financial year had any other disclosable interest in the shares of the Bank.

According to the register of Directors' interests, no rights to subscribe for shares in or debentures of the Bank were granted to any of the Directors or their immediate families, or exercised by them, during the financial year.

The Bank provided qualifying third party indemnity provisions to directors during the financial year 2009 and at the date of this report.

## SHARIA'A SUPERVISORY BOARD MEMBERS

The Sharia'a Supervisory Board (SSB) members are as follows:

- Dr. Abdul Sattar Abu Ghuddah – Chairman
- Sheikh Nizam Yacouby – Deputy Chairman
- Dr. Abdul Latif M. Al Mahmood

## ZAKAH

Zakah is an annual amount to be paid by Muslims to charity out of their savings. The Directors calculate that the zakah contribution payable by shareholders on their share of the Bank's earnings is 0.20p per share or £2.03 per thousand shares held based on the net assets method as detailed in the Accounting, Auditing and Governance Standards 2004-5 of the Accounting and Auditing Organisation for Islamic Financial Institutions.

### **POLITICAL CONTRIBUTIONS AND CHARITABLE DONATIONS**

The Bank made no political contributions during the year. Under the supervision of the SSB, receipts totalling £1,645 (which amount was deemed by the SSB to be non-sharia'a compliant income of the Bank) was paid to charitable causes during the year.

### **POLICY AND PRACTICE ON PAYMENT OF CREDITORS**

The Bank follows "The Better Payment Practice Code" published by the Department of Trade and Industry, regarding the making of payments to suppliers.

The Bank's policy is to agree terms of payment with suppliers and these normally provide for settlement within 30 days after the date of the invoice, except where other arrangements have been negotiated. It is the policy of the Bank to abide by the agreed terms of payment, provided the supplier performs according to the terms of the contract.

### **EVENTS SINCE THE BALANCE SHEET DATE**

The Directors confirm there are no significant events arising since the balance sheet date that should be reported to shareholders.

### **GOING CONCERN**

In approving the financial statements the Directors have reviewed the current and potential future business activities and financial position of the Bank, including an assessment of the capital adequacy and liquidity forecasts. Based upon this they are satisfied that the Bank has adequate resources to continue in business for the foreseeable future. For this reason the Directors continue to adopt the going concern basis in preparing the financial statements.

### **AUDITORS**

Resolutions concerning the appointment of auditors and authorising the Directors to set their remuneration will be proposed at the Annual General Meeting.

### **DIRECTORS' STATEMENT AS TO DISCLOSURE OF INFORMATION TO AUDITORS**

The Directors who were members of the Board at the time of approving the Directors' report are listed on pages 6 and 7. Having made enquiries of fellow Directors and of the Bank's auditors, each of the Directors confirms that:

- to the best of each Director's knowledge and belief, there is no information relevant to the preparation of the report of which the Bank's auditors are unaware; and
- each Director has taken all the steps a Director might reasonably be expected to have taken to be aware of relevant audit information and to establish that the Bank's auditors are aware of that information.

By order of the Board



Mohammed Abdul Mohaimin Chowdhury  
*Company Secretary*

9 March 2010

Registered Office:  
131 Finsbury Pavement  
London EC2A 1NT

### **COMPLIANCE WITH THE COMBINED CODE**

The Board considers that good corporate governance is central to achieving the Bank's objectives and has applied these principles in drawing up the Bank's risk management framework taking into consideration The Combined Code on Corporate Governance June 2008 published by the Financial Reporting Council ("The Combined Code").

### **THE BOARD AND ITS COMMITTEES**

The Bank is led by a Board comprising non-executive and executive Directors with wide experience of Islamic and conventional banking. The appointment of Directors is considered by the nominations committee and then the Board. Following the provisions in the Articles of Association, all Non-Executive Directors must stand for re-election by the shareholders at the first Annual General Meeting following their appointment and following that meeting must stand for re-election by the shareholders, at least every three years. Executive Directors normally retire at age 65, as required by their service agreements. Non-executive Directors are appointed for three-year renewable terms, which may be terminated by giving three months notice.

The Board is required to meet at least four times a year; in 2009 there were seven Board meetings. The Board has a programme designed to enable the Directors to review corporate strategy and the operations and results of the business and to discharge their duties within a framework of appropriate and effective controls relating to the assessment and management of risk.

The matters specifically referred to the Board for decision include the approval of the annual report and financial statements; the payment of dividends; the long-term objectives of the Bank; the strategies necessary to achieve these objectives; the Bank's budgets and plans; significant credit exposures; significant capital expenditure items; significant investments and disposals; the organisational structure of the Bank; the risk appetite of the Bank; the arrangements for ensuring that the Bank manages risk effectively; any significant change in accounting policies or practices; the appointment of the Bank's main professional advisers; and the appointment of senior executives within the organisation.

The Board has delegated to the Committees of the Bank the power to make decisions on operational matters, including those relating to credit, liquidity, operational and market risk, within an agreed framework.

All Directors have access to the services of the Company Secretary, and independent professional advice is available to the Directors at the Bank's expense, where they judge it necessary to discharge their duties as Directors.

The Board reviews and approves its composition and charter in order to set the risk management framework of the Bank at least annually. To assist the Board in executing its functions, it reviews and approves the composition and charters of the following Board sub-committees:

### **AUDIT COMMITTEE**

The Audit Committee comprises George Morton (chairman), Yusef Abu Khadra, Subhi Benkhadra and Zaher Al-Ajjawi. In discharging its duties, the committee is required to review the auditors' remuneration and, in discussion with them, to assess their independence and recommend their re-appointment at the Annual General Meeting. The committee also reviews the financial statements published in the name of the Board and the quality and acceptability of the related accounting policies, practices and financial reporting disclosures; the scope of work of the internal auditor, reports from the internal auditor and the adequacy of their resources; the effectiveness of the systems for internal control, risk management and compliance with financial services legislation and regulations; procedures by which staff may raise concerns in confidence; the results of the external audit and reports from the external auditor and their findings on accounting and internal control systems. The chairman of the committee has held a meeting with the auditors, without executives present, and a meeting with the internal auditor alone.

### **NOMINATION COMMITTEE**

The Nomination Committee, which comprises Salman Abbasi (chairman), Shabir Randeree and Mohammed Al Sarhan, reviews the composition of the Board, taking into account the skills, knowledge and experience of Directors and considers and makes recommendations to the Board on potential candidates for appointment as Directors. The committee also makes recommendations to the Board concerning the re-appointment of any independent non-executive Director by the Board at the conclusion of his or her specified term; the re-election of any Director by the shareholders under the retirement provisions of the Articles of Association; any matters relating to the continuation in office of a Director; and the appointment of any Director to executive or other office, other than the positions of Chairman and Chief Executive Officer, the recommendation for which would be considered at a meeting of the non-executive Directors regarding the position of Chief Executive Officer, and all the Directors regarding the position of Chairman.

The Nomination Committee evaluates, normally at least annually, the performance of the Board and its committees and makes appropriate recommendations to the Board. This is conducted through a self-assessment process that requires each Director to assess and rate the performance of the Board and its committees. The results of the exercise are considered by the Board and appropriate steps agreed and implemented to remedy any areas of deficiency or concern.

### REMUNERATION COMMITTEE

The Remuneration Committee, which comprises Shabir Randeree (chairman), Yusef Abu Khadra, Aabed Alzeera and Subhi Benkhadra, reviews the remuneration policy for senior management, to ensure that members of the executive are provided with appropriate incentives to encourage them to enhance the performance of the Bank and that they are rewarded for their individual contribution to the success of the organisation. It is also made aware of, and advises on, major changes to employee benefits schemes and agrees the policy for authorising claims for expenses from the Chief Executive Officer and the Chairman. All the non-executive Directors are invited to attend meetings if they wish, and they receive the minutes and have the opportunity to comment and have their views taken into account before the committee's decisions are implemented.

### BOARD EXECUTIVE COMMITTEE

The Board Executive Committee ("BEC") comprises Aabed Alzeera (chairman), George Morton, Shabir Randeree, Yusef Abu Khadra, Subhi Benkhadra and Mohammed Al Sarhan. The BEC assists the Board in fulfilling its investment risk management responsibilities; these responsibilities include determining the Bank's risk profile and ensuring that management remains within the Board's predetermined risk appetite. Meetings are held at least quarterly and include the Chief Executive Officer and Head of Risk Management by standing invitation. The terms of reference include reviewing capital adequacy, liquidity, credit risk, market risk, operational risk and anti-money laundering assessments and approvals under the Board's delegated authority.

### EXECUTIVE MANAGEMENT COMMITTEE

The Bank has an Executive Management Committee to assist the Chief Executive Officer in performing his duties. The Executive Management Committee membership comprises the Chief Executive Officer, Finance Director, the Head of Risk Management, the Managing Director of Treasury and Capital Markets, the Managing Director of Private Equity and Corporate Advisory and the Head of Legal and Sharia'a. Specifically, the committee considers the development and implementation of strategy,

operational plans, policies and budgets; the monitoring of operating and financial performance; the assessment and control of risk; the prioritisation and allocation of resources; and the monitoring of competitive forces in each area of operation. The committee, assisted by its sub-committees: the risk management, IT, human resources and asset and liability committees, also supports the Chief Executive Officer in ensuring the development, implementation and effectiveness of the Bank's risk management framework and the clear articulation of the Bank's risk policies, and in reviewing the Bank's aggregate risk exposures and concentrations of risk. The committee may have specific powers delegated to it by the Board from time to time and, following the exercise of these powers, it reports to the Board.

### MEETINGS AND ATTENDANCE

NO. OF MEETINGS IN YEAR	Board				
	Main Board	Audit Committee	Remuneration Committee	Nomination Committee	Executive Committee
Adnan Ahmed Yousif	7	5	4	3	8
Shabir Randeree	7		4	3	8
Salman Abbasi	6			3	
Yusef Abu Khadra	7	5	4		8
Zaher Al-Ajawi	5	4			
Mohammed Al Sarhan	5			2	7
Aabed Alzeera	7		4		8
Subhi Benkhadra	6	4	4		5
George Morton	7	5			5
John Weguelin *	3				
Keith McLeod	7				

\* resigned 21 August 2009

### SHAREHOLDERS

Under The Combined Code the Board appoints one of the independent non-executive Directors to be the Senior Independent Director. The Senior Independent Director, Mohammed Al Sarhan, is available to shareholders if they have concerns which contact through the normal channels of Chairman, Chief Executive Officer or Finance Director has failed to resolve or for which such contact is inappropriate. The Board ensures the Directors develop an understanding of the views of major shareholders by encouraging them to meet major shareholders and attend shareholder meetings; making them aware of views and feedback received from shareholders; and providing them with analysts' and brokers' briefings on the Bank.

**In the name of Allah, The Beneficent, The Merciful**

To the Shareholders of European Islamic Investment Bank plc ("EIIB")  
For the period 1 January 2009 to 31 December 2009 (the "Period")

*Assalamu Alaikum Wa Rahmat Allah Wa Barakatuh*

In compliance with our letters of appointment with EIIB, we are required to submit this report. Through our Sharia'a Audit Committee, we have reviewed the principles and the contracts relating to the transactions conducted by EIIB during the Period. We have conducted our review to form an opinion as to whether EIIB has complied with Sharia'a rules and principles and also with the specific fatwas, rulings and guidelines issued by us.

EIIB's management is responsible for ensuring that EIIB conducts its business in accordance with Sharia'a rules and principles. It is our responsibility to form an independent opinion, based on our review of the operations of EIIB, and to report to you.

We conducted our review which included examining, on a test basis, each type of transaction, the relevant documentation and procedures adopted by EIIB for the transaction. Based on this, we are of the opinion that the contracts, transactions and dealings entered into by EIIB during the Period that were reviewed are in compliance with Sharia'a rules and principles.

We beg Allah the Almighty to grant us all success and straight-forwardness.

*Wassalam Alaikum Wa Rahmat Allah Wa Barakatuh*

1 March 2010

Signed by the Sharia'a Supervisory Board of European Islamic Investment Bank plc



Dr. Abdul Sattar Abu Ghuddah  
(Chairman)



Sh. Nizam Yacoub  
(Deputy Chairman)



Dr. Abdul Latif Al Mahmood  
(Member)

## STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors are responsible for preparing the Annual Report and the financial statements on pages 16 to 65 in accordance with applicable law and regulations.

Company law requires the directors to prepare group and parent entity financial statements for each financial year. As required by the AIM Rules of the London Stock Exchange they are required to prepare the group financial statements in accordance with IFRSs as adopted by the EU and applicable law and have elected to prepare the parent entity financial statements on the same basis.

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the group and parent entity and of their profit or loss for that period. In preparing each of the group and parent entity financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the group and the parent entity will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent entity's transactions and disclose with reasonable accuracy at any time the financial position of the parent entity and enable them to ensure that its financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the group and to prevent and detect fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the Bank's website. Legislation in the UK governing the preparation and the dissemination of financial statements may differ from legislation in other jurisdictions.

## TO THE MEMBERS OF EUROPEAN ISLAMIC INVESTMENT BANK PLC

We have audited the financial statements of European Islamic Investment Bank plc ("Bank") for the year ended 31 December 2009 set out on pages 16 to 65. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards ("IFRSs") as adopted by the EU and, as regards the parent entity financial statements, as applied in accordance with the provisions of the Companies Act 2006.

This report is made solely to the Bank's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Bank's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Bank and the Bank's members, as a body, for our audit work, for this report, or for the opinions we have formed.

### RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

As explained more fully in the Directors' Responsibilities Statement set out on page 13, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

### SCOPE OF THE AUDIT OF THE FINANCIAL STATEMENTS

A description of the scope of an audit of financial statements is provided on the APB's web-site at [www.frc.org.uk/apb/scope/UKNP](http://www.frc.org.uk/apb/scope/UKNP).

### OPINION ON FINANCIAL STATEMENTS

In our opinion:

- the financial statements give a true and fair view of the state of the group's and of the parent entity's affairs as at 31 December 2009 and of the group's loss for the year then ended;
- the group financial statements have been properly prepared in accordance with IFRSs as adopted by the EU;

- the parent entity financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

### OPINION ON OTHER MATTER PRESCRIBED BY THE COMPANIES ACT 2006

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

### MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent entity, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent entity financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.



Paul Furneaux (Senior Statutory Auditor)  
for and on behalf of KPMG Audit Plc, Statutory Auditor  
Chartered Accountants  
One Canada Square  
London E14 5AG

9 March 2010

## **The Financial Statements**

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# CONSOLIDATED INCOME STATEMENT

for the year ended 31 December 2009

	Notes	2009 £	2008 £
<b>Income</b>			
Income from financing and investing activities	4	3,774,911	12,785,855
Returns to financial institutions and customers	5	(450,117)	(2,517,987)
<b>Net margin</b>		<b>3,324,794</b>	<b>10,267,868</b>
Foreign exchange gains	6	91,340	805,985
Trading income	7	309,813	242,970
Fees and commissions		-	787,143
Oil & gas gross loss		(355,930)	-
<b>Total operating income</b>		<b>3,370,017</b>	<b>12,103,966</b>
<b>Expenses</b>			
Fair value loss on assets designated as fair value through income statement	16	(4,134,525)	-
Provision for impairment of financing arrangements	14	(6,351,575)	(3,750,000)
Provision for impairment of available for sale securities	15	(7,030,988)	-
Impairment of goodwill	30.1	(954,077)	-
Staff costs	8	(4,709,722)	(5,016,059)
Depreciation and amortisation	18,19	(405,596)	(428,374)
Other operating expenses	9	(2,657,533)	(2,345,672)
Oil & gas overheads		(824,715)	-
<b>Operating (loss)/profit before tax</b>		<b>(23,698,714)</b>	<b>563,861</b>
Tax	11	1,519,399	(1,091,533)
<b>Loss for the year from continued operations</b>		<b>(22,179,315)</b>	<b>(527,672)</b>
<b>Loss after tax for the year from discontinued operations</b>	31	-	(14,285,451)
<b>Loss for the year</b>		<b>(22,179,315)</b>	<b>(14,813,123)</b>
<b>Attributable to:</b>			
Equity holders of the Bank		(22,013,425)	(14,813,123)
Non controlling interest		(165,890)	-
<b>Earnings per share</b>			
- basic and diluted	12	(1.22p)	(0.81p)
<b>Continuing operations</b>			
- basic and diluted	12	(1.22p)	(0.03p)

The notes on pages 24 to 65 form an integral part of the financial statements.

## CONSOLIDATED STATEMENT OF OTHER COMPREHENSIVE INCOME

for the year ended 31 December 2009

	2009	2008
	£	£
<b>Loss for the year</b>	<b>(22,179,315)</b>	<b>(14,813,123)</b>
<b>Other comprehensive income</b>		
Net change in fair value of available for sale financial assets	1,744,575	(3,890,474)
Net amount transferred to profit or loss	1,322,950	-
Income tax effect on the changes of available for sale financial assets	-	1,108,785
Exchange difference on net investment in foreign operations	183,728	-
<b>Other comprehensive income/(expense) for the period, net of income tax</b>	<b>3,251,253</b>	<b>(2,781,689)</b>
<b>Total comprehensive expense for the year</b>	<b>(18,928,062)</b>	<b>(17,594,812)</b>
<b>Attributable to:</b>		
Owners of the Bank	(18,785,201)	(17,594,812)
Non-controlling interest	(142,861)	-
	<b>(18,928,062)</b>	<b>(17,594,812)</b>

The notes on pages 24 to 65 form an integral part of the financial statements.

# CONSOLIDATED STATEMENT OF FINANCIAL POSITION

at 31 December 2009

	Notes	2009 £	2008 £
<b>Assets</b>			
Cash and balances with banks		685,495	972,540
Due from financial institutions	13	120,295,974	144,365,892
Financing arrangements	14	11,250,000	28,390,180
Available for sale securities - Sukuk	15	23,496,214	56,559,347
Available for sale securities - Equity		127,817	-
Financial assets designated at fair value	16	750,438	4,884,963
Fair value of foreign exchange agreements	17	30,091	20,012
Investment property	31	-	38,699,245
Plant and equipment	18	191,061	293,107
Intangible assets	19	415,512	683,261
Oil & gas properties	30.2	7,032,334	-
Other assets	20	1,747,471	1,975,217
Current tax asset	11	955,973	815,076
<b>Total assets</b>		<b>166,978,380</b>	<b>277,658,840</b>
<b>Liabilities</b>			
Due to financial institutions	21	21,273,067	107,084,431
Due to customers	22	1,009,533	2,728,522
Fair value of foreign exchange agreements	17	539,811	1,924,178
Other liabilities	23	2,837,556	2,504,209
Deferred tax liability	11	-	60,212
<b>Total liabilities</b>		<b>25,659,967</b>	<b>114,301,552</b>
<b>Shareholders' equity</b>			
Share capital	28	17,656,585	18,255,625
Share premium account	28	116,219,800	164,229,939
Capital redemption reserve	28	599,040	-
Fair value reserve		(161,161)	(3,228,686)
Foreign exchange reserve		160,699	-
Retained earnings		5,903,845	(15,899,590)
<b>Total equity attributable to the Bank's equity holders</b>		<b>140,378,808</b>	<b>163,357,288</b>
<b>Non-controlling interest</b>		<b>939,605</b>	<b>-</b>
<b>Total equity and liabilities</b>		<b>166,978,380</b>	<b>277,658,840</b>



Adnan Ahmed Yousif  
Chairman



Keith McLeod  
Acting Chief Executive Officer and Finance Director

The notes on pages 24 to 65 form an integral part of the financial statements.

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

for year ended 31 December 2009

	Share capital	Share premium account	Capital redemption reserve	Special reserve	Fair value reserve	Forex reserve	Retained earnings	Non controlling interest	Total equity - Group
	£	£	£	£	£	£	£	£	£
Balance at 1 January 2008	18,255,625	164,229,939	-	-	(446,997)	-	(1,119,160)	-	180,919,407
Share award	-	-	-	-	-	-	32,693	-	32,693
	<b>18,255,625</b>	<b>164,229,939</b>	-	-	<b>(446,997)</b>	-	<b>(1,086,467)</b>	-	<b>180,952,100</b>
Unrealised loss on available for sale investments					(3,890,474)	-	-	-	(3,890,474)
Tax effect adjusted					1,108,785	-	-	-	1,108,785
Loss for the year					-	-	(14,813,123)	-	(14,813,123)
Total comprehensive loss for the year					(2,781,689)	-	(14,813,123)	-	(17,594,812)
Balance at 31 December 2008	<b>18,255,625</b>	<b>164,229,939</b>	-	-	<b>(3,228,686)</b>	-	<b>(15,899,590)</b>	-	<b>163,357,288</b>
Balance at 1 January 2009	18,255,625	164,229,939	-	-	(3,228,686)	-	(15,899,590)	-	163,357,288
Creation of special reserve	-	(48,010,139)	-	48,010,139	-	-	-	-	-
Redemption/repurchase of shares	(599,040)	-	599,040	(4,193,279)	-	-	-	-	(4,193,279)
Non controlling interest arising on business combinations	-	-	-	-	-	-	-	1,082,466	1,082,466
	<b>17,656,585</b>	<b>116,219,800</b>	<b>599,040</b>	<b>43,816,860</b>	<b>(3,228,686)</b>	-	<b>(15,899,590)</b>	<b>1,082,466</b>	<b>160,246,475</b>
Net unrealised profit on available for sale securities					1,744,575	-	-	-	1,744,575
Impairment losses on available for sale investments transferred to income statement					1,322,950	-	-	-	1,322,950
Loss for the year					-	-	(22,013,425)	(165,890)	(22,179,315)
Foreign exchange adjustment					-	160,699	-	23,029	183,728
Transfer from Special Reserve				(43,816,860)	-	-	43,816,860	-	-
Total comprehensive loss for the year				(43,816,860)	3,067,525	160,699	21,803,435	(142,861)	(18,928,062)
Balance at 31 December 2009	<b>17,656,585</b>	<b>116,219,800</b>	<b>599,040</b>	-	<b>(161,161)</b>	<b>160,699</b>	<b>5,903,845</b>	<b>939,605</b>	<b>141,318,413</b>

The notes on pages 24 to 65 form an integral part of the financial statements.

# CONSOLIDATED STATEMENT OF CASH FLOW

for the year ended 31 December 2009

	Notes	2009 £	2008 £
<b>Cash flows from operating activities</b>			
Operating (loss)/profit on			
- continuing activities before tax		(23,698,714)	563,861
- discontinued operations		-	(14,285,451)
Adjusted for:			
Provision for impairment of the property portfolio	31	-	14,705,914
Provision for impairment of financial assets		14,336,640	3,750,000
Net loss on investment securities at fair value through income statement		4,134,525	-
Depreciation and amortisation	18,19	405,596	722,460
Charges for share awards	8	-	32,693
Net (increase)/decrease in operating assets:			
Collateral deposits		-	235,732
Due from financial institutions		24,069,917	53,405,223
Financing arrangements		10,788,605	(7,105,241)
Available for sale securities - Sukuk		29,421,992	(26,129,769)
Available for sale securities - Equity		(127,817)	-
Financial assets designated at fair value		-	(4,884,963)
Fair value of foreign exchange agreements		(1,394,446)	1,170,102
Investment property	31	38,699,245	-
Other assets		1,561,775	1,745,276
Net increase/(decrease) in operating liabilities:			
Due to financial institutions		(85,811,364)	(19,596,561)
Due to customers		(1,718,988)	(43,458)
Other liabilities		(163,258)	(2,087,890)
Taxation:			
Corporation tax recovered/(paid)		785,471	(1,790,000)
<b>Net cash inflow from operating activities</b>		<b>11,289,179</b>	<b>407,928</b>
<b>Cash flow from investing activities</b>			
Acquisition of subsidiaries, net of cash acquired		(7,347,144)	-
Purchase of plant and equipment	18	(15,878)	(28,478)
Purchase of intangible assets	19	(19,923)	(51,756)
<b>Net cash outflow from investing activities</b>		<b>(7,382,945)</b>	<b>(80,234)</b>
<b>Cash flow from financing activities</b>			
Redemption of shares		(4,193,279)	-
<b>Net cash outflow from financing activities</b>		<b>(4,193,279)</b>	<b>-</b>
<b>Net (decrease)/increase in cash and cash equivalents</b>		<b>(287,045)</b>	<b>327,694</b>
Cash and cash equivalents at the beginning of the year		972,540	644,846
<b>Cash and cash equivalents at the end of the year</b>		<b>685,495</b>	<b>972,540</b>

The notes on pages 24 to 65 form an integral part of the financial statements.

# COMPANY STATEMENT OF FINANCIAL POSITION

at 31 December 2009

	Notes	2009 £	2008 £
<b>Assets</b>			
Cash and balances with banks		459,065	652,867
Due from financial institutions	13	120,295,974	144,365,892
Financing arrangements	14	11,250,000	28,390,180
Available for sale securities – Sukuk	15	23,496,214	56,559,347
Available for sale securities – Equity		127,817	-
Financial assets designated at fair value	16	750,438	4,884,963
Investments in subsidiaries	30	6,345,002	-
Fair value of foreign exchange agreements	17	30,091	20,012
Plant and equipment	18	191,061	293,107
Intangible assets	19	415,512	683,261
Other assets	20	1,072,362	1,515,020
Current tax asset	11	955,973	815,076
<b>Total assets</b>		<b>165,389,509</b>	<b>238,179,725</b>
<b>Liabilities</b>			
Due to financial institutions	21	21,273,067	68,034,431
Due to customers	22	1,009,533	2,728,522
Fair value of foreign exchange agreements	17	539,811	1,924,178
Other liabilities	23	2,188,290	2,075,094
Deferred tax liability	11	-	60,212
<b>Total liabilities</b>		<b>25,010,701</b>	<b>74,822,437</b>
<b>Shareholders' equity</b>			
Share capital	28	17,656,585	18,255,625
Share premium account	28	116,219,800	164,229,939
Capital redemption reserve	28	599,040	-
Fair value reserve		(161,161)	(3,228,686)
Retained earnings		6,064,544	(15,899,590)
<b>Total equity attributable to the Bank's equity holders</b>		<b>140,378,808</b>	<b>163,357,288</b>
<b>Total equity and liabilities</b>		<b>165,389,509</b>	<b>238,179,725</b>



Adnan Ahmed Yousif  
Chairman



Keith McLeod  
Acting Chief Executive Officer and Finance Director

The notes on pages 24 to 65 form an integral part of the financial statements.

# COMPANY STATEMENT OF CHANGES IN EQUITY

for the year ended 31 December 2009

	Share capital	Share premium account	Capital redemption reserve	Special reserve	Fair value reserve	Retained earnings	Total Equity - Company
	£	£	£	£	£	£	£
Balance at 1 January 2008	18,255,625	164,229,939	-	-	(446,997)	(1,119,160)	180,919,407
Share award	-	-	-	-	-	32,693	32,693
	18,255,625	164,229,939	-	-	(446,997)	(1,086,467)	180,952,100
Unrealised loss on available for sale investments					(3,890,474)	-	(3,890,474)
Tax effect adjusted					1,108,785	-	1,108,785
Loss for the year					-	(14,813,123)	(14,813,123)
Total comprehensive loss for the year					(2,781,689)	(14,813,123)	(17,594,812)
<b>Balance at 31 December 2008</b>	<b>18,255,625</b>	<b>164,229,939</b>	<b>-</b>	<b>-</b>	<b>(3,228,686)</b>	<b>(15,899,590)</b>	<b>163,357,288</b>
Balance at 1 January 2009	18,255,625	164,229,939	-	-	(3,228,686)	(15,899,590)	163,357,288
Creation of special reserve	-	(48,010,139)	-	48,010,139	-	-	-
Redemption/ repurchase of shares	(599,040)	-	599,040	(4,193,279)	-	-	(4,193,279)
	17,656,585	116,219,800	599,040	43,816,860	(3,228,686)	(15,899,590)	159,164,009
Net unrealised profit on available for sale securities					1,744,575	-	1,744,575
Impairment losses on available for sale investments transferred to income statement					1,322,950	-	1,322,950
Loss for the year					-	(21,852,726)	(21,852,726)
Transfer from Special Reserve				(43,816,860)	-	43,816,860	-
Total comprehensive loss for the year				(43,816,860)	3,067,525	21,964,134	(18,785,201)
<b>Balance at 31 December 2009</b>	<b>17,656,585</b>	<b>116,219,800</b>	<b>599,040</b>	<b>-</b>	<b>(161,161)</b>	<b>6,064,544</b>	<b>140,378,808</b>

The notes on pages 24 to 65 form an integral part of the financial statements.

# COMPANY STATEMENT OF CASH FLOW

for the year ended 31 December 2009

	Notes	2009 £	2008 £
<b>Cash flows from operating activities</b>			
Operating (loss)/profit before tax		(23,372,145)	563,861
Adjusted for:			
Provision for impairment of financial assets		13,382,561	3,750,000
Net loss on investment securities at fair value through income statement		5,942,657	-
Depreciation and amortisation	18,19	405,596	428,374
Charges for share awards	8	-	32,693
Net (increase)/decrease in operating assets:			
Collateral deposits		-	235,732
Due from financial institutions		24,069,917	53,405,223
Financing arrangements		10,788,605	(7,105,241)
Available for sale securities – Sukuk		29,421,992	(26,129,769)
Available for sale securities – Equity		(127,817)	-
Financial assets designated at fair value		-	(4,884,963)
Fair value of foreign exchange agreements		(1,394,446)	1,170,102
Other assets		653,157	692,646
Net increase/(decrease) in operating liabilities:			
Due to financial institutions		(46,761,364)	(19,596,561)
Due to customers		(1,718,988)	(43,458)
Other liabilities		113,196	(556,817)
Taxation:			
Corporation tax recovered/(paid)		785,471	(1,790,000)
<b>Net cash inflow from operating activities</b>		<b>12,188,412</b>	<b>171,822</b>
<b>Cash flow from investing activities</b>			
Acquisition of subsidiaries	30	(8,153,134)	-
Purchase of plant and equipment	18	(15,878)	(28,478)
Purchase of intangible assets	19	(19,923)	(51,756)
<b>Net cash outflow from investing activities</b>		<b>(8,188,935)</b>	<b>(80,234)</b>
<b>Cash flow from financing activities</b>			
Redemption of shares		(4,193,279)	-
<b>Net cash outflow from financing activities</b>		<b>(4,193,279)</b>	<b>-</b>
<b>Net (decrease)/increase in cash and cash equivalents</b>		<b>(193,802)</b>	<b>91,588</b>
Cash and cash equivalents at the beginning of the year		652,867	561,279
<b>Cash and cash equivalents at the end of the year</b>		<b>459,065</b>	<b>652,867</b>

The notes on pages 24 to 65 form an integral part of the financial statements.

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 1 PRINCIPAL ACTIVITIES, DEFINITIONS AND AUTHORISATION OF THE FINANCIAL STATEMENTS

European Islamic Investment Bank plc ('EIIIB' or 'Bank') was incorporated as the first independent, UK based Islamic investment bank managed on a wholly Sharia'a compliant basis. The activities of the Bank are focused on servicing clients internationally through the provision of services encompassing trading and investing in Islamic securities, treasury services and structured products (Treasury and Capital Market activities), Private Equity and Corporate Advisory.

The Bank is a company incorporated in the UK which was established on 11 January 2005 and received authorisation from the FSA on 8 March 2006 to carry on activities as an investment bank.

The consolidated financial statements of the Bank as at and for the year ended 31 December 2009 comprise the Bank and its subsidiaries (together referred to as the "Group" and individually as "Group entities").

The following terms are used in the financial statements:

**Murabaha** (notes 13, 14 & 21) is a sale of goods at a cost plus an agreed profit mark up under which a party (the seller) purchases goods at cost price from a supplier and sells the goods to another (the buyer) at a cost plus an agreed mark up. Commodity murabaha, whereby commodities are bought and sold are a common form of Islamic financing transaction.

**Sukuk** (note 15) are certificates of equal value representing undivided shares in ownership of tangible assets, usufruct and services or (in the ownership of) the assets of particular projects or special investment activities. Sukuk are usually tradable and yield periodic profit distributions.

**Wakala** (notes 13, 21 & 22) means agency and can be used in an arrangement whereby one party (the principal) places funds with another (the agent) for investment by the agent on the principal's behalf in return for an agreed fee or commission.

The financial statements of European Islamic Investment Bank plc for the year ended 31 December 2009 were authorised for issue by the Board of Directors on 9 March 2010.

## 2 ACCOUNTING POLICIES

### 2.1 Basis of preparation

The financial statements have been prepared under the historical cost accounting convention, except for financial assets and liabilities stated at their fair value comprising: available for sale securities, financial assets designated at fair value, fair value of foreign exchange agreements and the investment property at fair value (note 31).

As permitted by section s.408 of the Companies Act 2006 the income statement of the parent entity is not presented as part of the financial statements. The parent entity's loss after tax for the year ended 31 December 2009 was £21,852,726 (2008: loss £14,813,123).

### 2.2 Compliance with International Financial Reporting Standards

The consolidated financial statements and the financial statements of the Bank have been prepared in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union.

### 2.3 Accounting policy, disclosures and changes to the accounting policies

The accounting policies applied by the Group in these consolidated financial statements are the same as those applied by the Group in financial statements as at and for the year ended 31 December 2008 except that the following new accounting standards and amendments have been adopted from 1 January 2009.

#### 2.3.1 Accounting for business combinations

The Group has adopted IFRS 3 Business Combinations (2008) and IAS 27 Consolidated and Separate Financial Statements (2008) for business combinations occurring in the financial year starting 1 January 2009. Business combinations occurring on or after 1 January 2009 are accounted for by applying the acquisition method. This has not had an impact upon the Group in respect of prior years but has been applied to new combinations during the period.

Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, the Group takes into consideration potential voting rights that are currently exercisable. The acquisition date is the date on which control is transferred to the acquirer. Judgement is applied in determining the acquisition date and determining whether control is transferred from one party to another.

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## *Acquisitions on or after 1 January 2009*

For acquisition on or after 1 January 2009, the Group measures goodwill as the fair value of the consideration transferred including the recognised amount of any non-controlling interest in the acquiree, less the net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed, all measured as of the acquisition date. When the excess is negative, a bargain purchase gain is recognised immediately in the profit or loss.

The Group elects on a transaction-by-transaction basis whether to measure non-controlling interest at its fair value, or at its proportionate share of the recognised amount of the identifiable net assets, at the acquisition date.

Transaction costs, other than those associated with the issue of debt or equity securities, that the Group incurs in connection with a business combination are expensed as incurred.

## *Acquisitions prior to 1 January 2009*

For acquisitions prior to 1 January 2009, goodwill represents the excess of the cost of the acquisition over the Group's interest in the recognised amount (generally fair value) of the identifiable assets, liabilities and contingent liabilities of the acquiree. When the excess was negative, a bargain purchase gain was recognised immediately in the profit or loss.

Transaction costs, other than those associated with the issue of debt or equity securities, that the Group incurred in connection with business combinations were capitalised as part of the cost of acquisitions.

### **2.3.2 Determination and presentation of operating segments**

The Group has early adopted IFRS 8 *Operating Segments* as of 1 January 2009. This Standard requires the presentation of financial information for segments based on information that is internally presented to the decision making function for the purposes of resource allocation and performance assessment.

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses. Segmental reporting was governed under IAS 14 *Segment Reporting*, until 31 December 2008. However, the adoption of IFRS 8 has had no significant impact on the Group as the operating segments have always been identified based on the internal reporting structure.

### **2.3.3 Presentation of financial statements**

The Group has applied revised IAS 1 *Presentation of Financial Statements* (2007), which became effective as of 1 January 2009. Comparative information has been re-presented so that it also is in conformity with the revised standard. The change in accounting policy only impacts presentation aspects of the financial statements.

### **2.3.4 Disclosure pertaining to fair values and liquidity risk for financial instruments**

The Group has applied *Improving Disclosures about Financial Instruments* (Amendments to IFRS 7) issued in March 2009, that require enhanced disclosures about fair value measurements and liquidity risk in respect of financial instruments.

The amendments require that fair value measurement disclosures use a three-level fair value hierarchy that reflects the significance of the inputs used in measuring fair values of financial instruments. Specific disclosures are required when fair value measurements are categorised as Level 3 (significant unobservable inputs) in the fair value hierarchy. The amendments require that any significant transfers between Level 1 and Level 2 of the fair value hierarchy be disclosed separately, distinguishing between transfers into and out of each level. Furthermore, changes in valuation techniques from one period to another, including the reasons therefore, are required to be disclosed for each class of financial instruments.

Revised disclosures in respect of fair values of financial instruments are included in note 33.

Further, the definition of liquidity risk has been amended and it is now defined as the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset.

Revised disclosures in respect of liquidity risk are included in note 34.

### **2.4 Standards and interpretations issued but not yet effective**

New standards, amendments and interpretations to existing standards which have been published by IASB and IFRIC with an effective date after the date of these financial statements and, which the Bank has not early adopted, are as follows:

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- IAS 24 (Amendments) *Related party transactions* (effective date 1 January 2011)
- IAS 32 *Presentation: Classification of Rights issues* (effective 1 February 2010)
- IAS 39 *Financial Instruments: Recognition and Measurement - Eligible Hedged Items* (effective 1 July 2009\*)
- IFRS 1 (Amendments) *First-time Adoption of International Financial Reporting Standards* (effective 1 July 2009\*)
- IFRS 2 (Amendments) *Share based payments* (effective 1 January 2010)
- IFRS 9 *Financial Instruments* (effective 1 January 2013)
- Improvements to IFRS 2009– IFRS 2 (*Scope*), IFRS 8 (*Disclosure about segment assets*), IAS 1 (*Current/non-current classification of convertible instruments*), IAS 18 (*Principal or agent*) (effective 1 January 2010)

The Group anticipates that the accounting pronouncements which have not been early adopted will have no material effect on the financial statements except for IFRS 9. The Group is currently in the process of evaluating the potential effect of this standard.

\* for financial periods starting on or after this date

## 2.5 Basis of consolidation

### Subsidiaries

The consolidated financial statements of the Bank comprise the financial statements of the European Islamic Investment Bank plc and the entities the Bank controls. Control exists where the Bank has the power to govern the financial and operating policies of the entity so as to obtain benefits from its activities. Controlled entities are consolidated from the date on which control is transferred to the Bank and they are deconsolidated from the date the control ceases. All intra-group balances, transactions, income and expenses and profits and losses resulting from intra-group transactions are eliminated in full upon consolidation.

### Associates

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Investments that are held as part of the Group's investment portfolio are carried in the balance sheet at fair value even though the Group may have significant influence over those companies. This treatment is permitted by IAS 28 Investment in Associates, which requires investments held by venture capital organisations to be excluded from its scope where those investments are designated, upon initial recognition, as at fair value through profit or loss and accounted for in accordance with IAS 39, with changes in fair value recognised in the

income statement in the period of the change. The Group has no interests in associates through which it carries on its business.

## 2.6 Going concern

In approving the financial statements the Directors have reviewed the current and potential future business activities and financial position of the Group, including an assessment of the capital adequacy and liquidity forecasts.

EIIB's core activities suffered due to the depressed market conditions, lower base rate regime, fair value losses and impairment charges which arose mainly due to the global economic crisis. However the Bank remained well capitalised, thinly leveraged, highly liquid and adequately hedged on most financial market related risks, providing it with the necessary resources for good growth prospects.

EIIB had total assets of £167m (2008:£278m) and a minimum regulatory capital requirement thereon of £13.6m (2008: £24m) as at 31 December 2009. The Capital Base at 31 December 2009 stood at £132.9m (2008: £163m) which is 9.8 times (2008: 6.8 times) the required minimum.

The balance sheet of EIIB is highly liquid and the position is managed on a day to day basis. On 31 December 2009, as measured using the FSA's liquidity calculation, the net cash excess (calculated as a percentage of deposits) was +159% (2008: +20%) in the 8 days and under category, and +361% (2008: +48%) in the 1 month and under category, against minimum requirements of 0% and -5% respectively.

Based upon the above, the Directors are satisfied that the Group has adequate resources to continue in business for the foreseeable future. For this reason the Directors continue to adopt the going concern basis in preparing the financial statements.

## 2.7 Significant accounting judgements and estimates

In applying accounting policies, management has to exercise its judgement and make estimates in determining the amounts recognised in the financial statements. However, the nature of estimation means that actual outcomes could differ from those estimates. The most significant are set out below.

### 2.7.1 Fair value of financial instruments

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date.

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

When available, the Group measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active, the Group establishes fair value using a valuation technique. Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties (if available), reference to the current fair value of other instruments that are substantially the same, discounted cash flow analyses and option pricing models. The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates specific to the Group, incorporates all factors that market participants would consider in setting a price, and is consistent with accepted economic methodologies for pricing financial instruments. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument. The Group calibrates valuation techniques and tests them for validity using prices from observable current market transactions in the same instrument or based on other available observable market data.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price, i.e. the fair value of the consideration given or received, unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When transaction price provides the best evidence of fair value at initial recognition, the financial instrument is initially measured at the transaction price and any difference between this price and the value initially obtained from a valuation model is subsequently recognised in profit or loss on an appropriate basis over the life of the instrument but not later than when the valuation is supported wholly by observable market data or the transaction is closed out.

Assets and long positions are measured at a bid price; liabilities and short positions are measured at an asking price. Where the Group has positions with offsetting risks, mid-market prices are used to measure the offsetting risk positions and a bid or asking price adjustment is applied only to the net open position as appropriate. Fair values reflect the credit risk of the instrument and include adjustments to take account of

the credit risk of the Group entity and the counterparty where appropriate. Fair value estimates obtained from models are adjusted for any other factors, such as liquidity risk or model uncertainties, to the extent that the Group believes a third-party market participant would take them into account in pricing a transaction.

The Directors consider the fair value of the financial assets and liabilities held at amortised cost to be materially equal to the carrying value of those assets and liabilities in the balance sheet as at 31 December 2009.

## 2.7.2 Provisions for impairment of financial assets

At each reporting date the Group assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. A financial asset or a group of financial assets is (are) impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s), and that the loss event has an impact on the future cash flows of the asset(s) that can be estimated reliably.

Objective evidence that financial assets (including equity securities) are impaired can include significant financial difficulty of the borrower or issuer, default or delinquency by a borrower, restructuring of a loan or advance by the Group on terms that the Group would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group. In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

The Group considers evidence of impairment for assets carried at amortised cost at both a specific asset and collective level. All individually significant assets carried at amortised cost are assessed for specific impairment. All individually significant assets carried at amortised cost found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Assets carried at amortised cost that are not individually significant are collectively assessed for impairment by grouping together assets carried at amortised cost with similar risk characteristics. In assessing collective impairment the Group uses statistical modelling of historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

such that the actual losses are likely to be greater or less than suggested by historical modelling. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

Impairment losses on assets carried at amortised cost are measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the asset's original effective profit rate. Impairment losses are recognised in profit or loss and reflected in an allowance account. Profit on impaired assets continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

Impairment losses on available-for-sale investment securities are recognised by transferring the cumulative loss that has been recognised in other comprehensive income to profit or loss as a reclassification adjustment. The cumulative loss that is reclassified from other comprehensive income to profit or loss is the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less any impairment loss previously recognised in profit or loss. Changes in impairment provisions attributable to time value are reflected as a component of profit income.

If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed, with the amount of the reversal recognised in profit or loss. However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognised in other comprehensive income. The Group writes off certain investment securities when they are determined to be uncollectible.

### 2.7.3 Exploration and evaluation expenditure

The Group applies IFRS 6 "Exploration for and Evaluation of Mineral Resources". Oil and gas exploration activity is accounted for in accordance with the successful efforts method. Accordingly, mineral interests are capitalised as intangible assets when acquired. These acquired interests are tested for impairment on a regular basis, based on the results of the exploratory activity and the management's evaluation thereof.

### 2.7.4 Impairment of other non-financial assets

The carrying amounts of the Group's non-financial assets, other than investment property and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated. For goodwill and intangible assets that have indefinite useful lives or that are not yet available for use, the recoverable amount is estimated each year at the same time.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit" or "CGU"). Subject to an operating segment ceiling test, for the purposes of goodwill impairment testing, CGUs to which goodwill has been allocated are aggregated so the level at which impairment is tested reflects the lowest level at which goodwill is monitored for internal reporting purposes. Goodwill acquired in a business combination is allocated to groups of CGUs that are expected to benefit from the synergies of the combination.

The Group's corporate assets do not generate separate cash inflows. If there is an indication that a corporate asset may be impaired, then the recoverable amount is determined for the CGU to which the corporate asset belongs.

An impairment loss is recognised if the carrying amount of an asset or a CGU exceeds its recoverable amount. Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the CGU and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis. An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An

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for the year ended 31 December 2009

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

## 2.7.5 Provisions for impairment of investment property

The Group assesses periodically whether there is any indication that the investment properties are impaired. If any such indication exists, an estimate is made of the recoverable amount of the asset and the resulting impairment loss. The recoverable amount of an asset is the higher of its fair value less cost to sell, and its value in use. Value in use is the present value of future cash flows from the assets discounted at a rate that reflects market returns adjusted for risks specific to the assets. If the recoverable amount of an asset is less than its carrying value, an impairment loss is recognised immediately in the income statement.

## 2.8 Summary of significant accounting policies

### 2.8.1 Foreign currency

The financial statements are presented in Sterling, which is the Bank's functional and presentation currency. Transactions in foreign currencies are initially recorded at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated into the functional currency at the rate of exchange ruling at the balance sheet date. Non-monetary assets and liabilities are translated into Sterling at the effective historical rate used on the date of initial recognition. All differences are taken to the income statement.

In the consolidated financial statements, the assets and liabilities of subsidiaries whose functional currency is not Sterling, are translated into the Group's presentation currency at the rate of exchange ruling at the balance sheet date. The income and expenses of these foreign operations are translated at the average rate of exchange for the reporting period. Foreign currency differences on the translation of foreign operations are recognised, via other comprehensive income, in equity in the *Foreign exchange reserve*. If the subsidiaries are not wholly owned, the relevant proportionate share of the difference is allocated to the non-controlling interest.

### 2.8.2 Revenue recognition

*a Sukuk, murabaha and wakala income and expense*  
Sukuk, murabaha and wakala are Islamic financing transactions. Sukuk are certificates of equal value representing undivided shares in ownership of tangible assets, usufruct and services or (in the ownership of) the assets of particular projects or special investment activities. Murabaha is a contract for sale or purchase of goods where there is an agreed mark-up and deferred settlement. Wakala derives income and expense in the form of agency fee or commission. Income and expense for these arrangements are recognised on an effective yield basis over the periods of the contracts. The calculation of income and expense include any fees and incremental costs that are directly attributable to the financial instrument and are an integral part of the purchase or sale.

#### *b Trading income*

Trading income consists of realised profits and losses on Sukuk and equity *Available for sale securities*.

#### *c Fees and commission income*

Fees and commissions which are not recognised on an effective yield basis over the life of the financial instrument to which they relate, such as fees for negotiating transactions for third parties and underwriting fees and commission, are recognised in revenue when it is probable that the economic benefit will flow to the Bank. This will normally be from the point at which the act to which the fees and commissions relate has been completed.

#### *d Rental income*

Rental income arising from operating leases on properties held within Investment property is recognised on a straight-line basis over the life of the lease.

#### *e Dividend income*

Dividend income is recognised in profit or loss when the Group becomes entitled to the dividend. There was no dividend recognised in 2009.

### 2.8.3 Cash and cash equivalents

The captions *Cash and cash equivalents* and *Cash and balances with banks* represent cash and current account balances with banks and clearing exchanges, all held in interest-free accounts.

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 2.8.4 Financial instruments

### a Recognition of financial instruments

Financial instruments are recognised in the balance sheet on the trade date, that is, the date on which the Bank commits to buy or sell the financial instrument. All financial instruments are recognised initially at fair value. In the case of financial instruments not recognised at fair value through the income statement, that value will include direct costs of acquisition or issue. For financial instruments carried at fair value through the income statement, transaction costs are expensed immediately.

### b Due from financial institutions, Financing arrangements, Due to financial institutions and Due to customers

Financial assets included within *Due from financial institutions* and *Financing arrangements*, as well as financial liabilities included within *Due to financial institutions* and *Due to customers* comprise non-derivative financial assets with fixed or determinable repayments that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not designed as 'available for sale securities' or 'financial assets designated at fair value'. Financial assets included under these captions are initially recognised at fair value plus any directly related transaction costs. They are subsequently measured at amortised cost less any impairment losses. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the effective rate of return. The amortisation is included in *Income from financing and investing activities* and *Returns to financial institutions and customers* in the income statement.

At each reporting date the Bank reviews the carrying values of its financial assets; a financial asset is considered to be impaired if there is objective evidence of events since initial recognition of the asset that will adversely affect the amount or timing of future cash flows from the asset. The amount of the impairment loss will be the difference between the carrying value of the financial asset and the present value of the estimated future cash flows. The amount of the impairment loss will be recognised in the income statement, and the carrying value of the financial asset will be written down and the impairment loss allowance will be recognised in a reserve for that purpose. Where subsequent events indicate that the impairment loss allowance is not required, or not required in full, the loss allowance made will be reversed.

### c Available for sale securities

Available-for-sale investments are investments that are designated as available for sale or are not classified as another category of financial assets. These include Sukuk and equity (quoted). The intent to hold the securities and the illiquid nature of the Sukuk market make the designation as available for sale ("AFS") the most appropriate. The Bank disposes of positions from time to time to rebalance the portfolio, to reduce exposures to concentration risk, or where it believes market conditions merit such a sale.

AFS securities are recognised at cost at the point of acquisition. Cost being the fair value of the investment including any acquisition charges. AFS securities are then carried in the balance sheet at fair value. Income accruals on AFS securities are recognised in the income statement. Changes in the fair value are recognised directly in equity in the *Fair value reserve* in the accounting period in which they arise. Where the value of a security is considered to be impaired, the losses are recognised in the income statement; otherwise, the gains and losses previously recognised in equity are recognised through the income statement when the investment matures or is sold; these are included under *Trading income*. Fair value gains and losses are recognised in equity net of any tax effect.

### d Financial assets designated at fair value

Private equity investments managed and evaluated on a fair value basis in accordance with an agreed investment strategy and reported to key personnel on that basis are classified under this category. These assets are recognised initially at fair value and subsequent gains and losses arising from changes in the fair value are recognised directly in the income statement.

Financial assets classified in this category are designated by management on initial recognition given that the financial assets are managed and their performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy.

### e Foreign exchange commitments

The valuation of forward foreign exchange commitments held at fair value through the income statement is recognised in the balance sheet under Fair value of foreign exchange agreements on either the asset or liability side of the balance sheet dependent on whether the valuation is positive or negative respectively. Revaluation gains and losses are included in the income statement under Foreign exchange gains and losses.

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 2.8.5 Investments in subsidiaries

The Bank's investments in subsidiaries are designated for recognition and measurement in the financial statements as 'fair value through income statement'. Accordingly these assets are fair valued using suitable valuation techniques and the gain or loss is accounted in the income statement of the parent entity.

## 2.8.6 Oil and gas properties

EIIB follows the successful efforts method of accounting for oil and natural gas costs. Accordingly all costs incurred are capitalised at initial measurement and are subsequently tested for impairment.

Geological and geophysical costs, including seismic surveys for exploration purposes are expensed as incurred.

Mineral interests are capitalised as intangible assets when acquired. These acquired interests are tested for impairment on a regular basis, property-by-property, based on the results of the exploratory activity and the management's evaluation.

In the event of a discovery, the unproved mineral interests are transferred to proved mineral interests at their net book value as soon as proved reserves are booked.

Exploratory wells are tested for impairment on a well-by-well basis and accounted for as follows:

- Costs of exploratory wells which result in proved reserves are capitalised and then depreciated using the unit-of-production method based on proved developed reserves; Costs of dry exploratory wells and wells that have not found proved reserves are charged to expense;
- Costs of exploratory wells are temporarily capitalised until a determination is made as to whether the well has found proved reserves if both of the following conditions are met:
  - The well has found a sufficient quantity of reserves to justify its completion as a producing well, if appropriate, assuming that the required capital expenditures are made;
  - The Group is making sufficient progress assessing the reserves and the economic and operating viability of the project. This progress is evaluated on the basis of indicators such as whether additional exploratory works are under way or firmly planned (wells, seismic or significant studies), whether costs are being incurred for development studies and whether the Group is waiting for governmental or other third-party authorisation of a proposed project,

or availability of capacity on an existing transport or processing facility.

Costs of exploratory wells not meeting these conditions are charged to expense.

## 2.8.7 Investment property

The investment properties, accounted under IAS40, are reported at original cost (including transaction costs and taxes) less depreciation and at each reporting date the Group assesses whether there is any indication that the Investment properties are impaired. If any such indication exists, the Group estimates the recoverable amount of the asset and the impairment loss if any. The recoverable amount of an asset is the higher of its fair value less cost to sell, and its value in use. Value in use is the present value of future cash flows from the assets discounted at a rate that reflects market returns adjusted for risks specific to the assets. If the recoverable amount of an asset is less than its carrying value, an impairment loss is recognised immediately in income statement and the carrying value of the asset reduced by the amount of the loss.

Following the reclassification of the property portfolio as a 'discontinued operation' the Bank sold its property vehicle Pan European Islamic Real Estate Fund ('PEIREF') during December 2009. The discontinued activity was accounted for under IFRS 5 'Non-current assets held for sale and discontinued operations' in the Bank's interim financial statements (June 2009).

## 2.8.8 Plant and equipment

Plant and equipment is stated at cost less accumulated depreciation and impairment losses if any. Depreciation is provided on a straight line basis over estimated useful lives as follows:

Leasehold improvements	5 years
Fixtures, fittings and office equipment	5 years
Computer hardware	3 years

This excludes oil and gas properties shown in Note 30.

## 2.8.9 Intangible assets

Intangible assets consist of computer licences and software development costs including capitalised staff costs. Intangible assets are stated at cost less accumulated amortisation and impairment losses if any. Amortisation is provided on a straight line basis over a current estimated useful life of five years.

This excludes oil and gas related intangible assets shown in Note 30.

# NOTES TO THE FINANCIAL STATEMENTS

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## 2.8.10 Operating leases

Operating lease rentals are charged to the income statement on a straight line basis over the period of the lease. The charge in respect of the premises is after taking into account the rent free period.

## 2.8.11 Pension cost

The Bank operates a defined contribution pension scheme for all staff. The cost of the scheme is equal to the contributions payable to the scheme for the accounting period and is recognised within *Staff costs* in the income statement. The Bank has no further obligation once the contributions have been paid.

## 2.8.12 Share-based payments

EIIB engages in equity settled share based transactions in respect of services received from certain of its employees. The fair value of the services received is measured by reference to the fair value of the shares or the share options granted on the date of the grant. The cost of the employee services received in respect of the shares or share options granted is recognised in the income statement over the period that the services are received, which is the vesting period. Two share based payment schemes were in operation as at 31 December 2009.

### *a Directors and SSB members share based payment scheme*

The Bank made a share-based award to non-executive Directors and Sharia'a supervisory board (SSB) members whereby shares were granted in lieu of annual fees. The fair value of the shares allotted is expensed on a straight-line basis over the period of the services received. This scheme has expired and all shares have vested.

### *b Employee share incentive plan (ESIP)*

ESIP is designed to reward the employees for their current performance and is generally included as a part of the annual incentive payment. The reward may include a matching share element with a vesting period of more than one accounting period, subject to the employee's continuing employment with EIIB. These shares are valued at the date of the grant and amortised over the vesting period.

### *c Employee share option plan (ESOP)*

The value of options granted under this scheme are determined using option pricing models, which takes into account the exercise price of the option, the current share price, the risk free rate of return, the expected volatility of the share price over the life of the option and other relevant factors.

## 2.8.13 Taxation

Tax on the profit or loss for the year comprises current and deferred tax. Tax is recognised in the income statement except to the extent that it relates to items recognised directly in shareholders' equity, in which case it is recognised in shareholders' equity.

### *a Current tax*

Current tax is provided on taxable profits at the current rate.

### *b Deferred tax*

Deferred tax is recognised on temporary differences between the carrying amount of assets and liabilities in the balance sheet and the amount attributed to such assets and liabilities for tax purposes. Deferred tax liabilities are recognised for all taxable temporary differences and deferred tax assets are recognised to the extent it is probable that future taxable profits will be available against which deductible temporary differences can be utilised.

## 2.9 Comparatives

Certain amounts in the 2008 comparatives have been reclassified to conform to the current presentation. Such reclassification did not affect the overall financial position at 31 December 2008 or cash flow statement nor did it impact the previously reported loss or retained earnings.

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 3 SEGMENTAL INFORMATION

The Group has two reporting segments as at the end of 2009, the "Treasury and Capital Markets" division and the "Private Equity and Corporate Advisory" division, which are the Group's strategic business units ("SBU"). These SBU offer different products and services, and are managed separately based on the Group's management and internal reporting structure. A description of the activities of these divisions can be found in the "Operating and Financial Review" (page 4). For each SBU, the Group's management committees and the Board review internal management reports on a monthly basis.

The Treasury and Capital Markets unit became fully active in April 2006 following FSA authorisation. The majority of the cost base, and the assets and liabilities of the Bank have been deployed in support of that business unit. The Real Estate division was discontinued during 2009 (note 31). The Private Equity and Corporate Advisory division was launched in 2008 and the division had made two investments by 31 December 2009.

Information regarding the results of each reportable segment is included below. Performance is measured based on segment profit before tax and is reviewed by Group executive management and the board of directors. Segment results include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

	Treasury and Capital Markets	Real Estate (Discontinued)	Private Equity and Corporate Advisory	Total
	£	£	£	£
2009				
Revenue from external customers	4,176,064	1,991,000	69,884	6,236,948
Returns to external customers	(450,117)	(1,779,000)	-	(2,229,117)
Costs associated with Real Estate	(212,000)	-	(212,000)	-
Gross loss of oil & gas operations	-	-	(425,814)	(425,814)
Operating income	3,725,947	-	(355,930)	3,370,017
<b>Divisional loss before tax</b>	<b>(13,851,082)</b>	<b>-</b>	<b>(8,952,999)</b>	<b>(22,804,081)</b>
Unallocated*				(894,633)
Operating loss before tax				(23,698,714)
<i>Fair value movement</i>	-	-	(4,134,525)	(4,134,525)
<i>Impairment of assets</i>	(13,382,563)	-	(954,077)	(14,336,640)
	(13,382,563)	-	(5,088,602)	(18,471,165)
Depreciation and amortisation	(304,197)	-	(101,399)	(405,596)
<b>Segment assets</b>	<b>158,162,900</b>	<b>-</b>	<b>8,815,480</b>	<b>166,978,380</b>
<b>Segment liabilities</b>	<b>24,791,873</b>	<b>-</b>	<b>868,094</b>	<b>25,659,967</b>
Capital expenditure				
Plant and equipment	11,490	-	4,388	15,878
Intangible assets	13,947	-	5,976	19,923

\* Centrally incurred costs are allocated according to usage

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 3 SEGMENTAL INFORMATION continued

2008	Treasury and Capital Markets £	Real Estate (Discontinued) £	Private Equity and Corporate Advisory £	Total £
Revenue from external customers	14,621,953	3,693,527	-	18,315,480
Returns to external customers	(2,517,987)	(2,555,972)	-	(5,073,959)
Operating income	12,103,966	1,137,555	-	13,241,521
<b>Divisional profit/(loss) before tax</b>	<b>2,926,301</b>	<b>(15,704,317)</b>	<b>(943,574)</b>	<b>(13,721,590)</b>
Impairment of assets	(3,750,000)	(14,705,914)	-	(18,455,914)
Depreciation and amortisation	(376,791)	(327,478)	(18,191)	(722,460)
<b>Segment assets</b>	<b>232,940,220</b>	<b>39,551,255</b>	<b>5,167,365</b>	<b>277,658,840</b>
<b>Segment liabilities</b>	<b>74,822,437</b>	<b>39,479,115</b>	<b>-</b>	<b>114,301,552</b>
Capital expenditure				
Plant and equipment	18,061	6,779	3,638	28,478
Intangible assets	46,910	3,205	1,641	51,756

## 4 INCOME FROM FINANCING AND INVESTING ACTIVITIES

Group and Bank	2009 £	2008 £
Due from financial institutions - murabaha and wakala	1,376,022	7,487,206
Financing arrangements - murabaha	1,184,794	3,148,045
Available for sale investments - Sukuk	1,214,095	2,150,604
	<b>3,774,911</b>	<b>12,785,855</b>

## 5 RETURNS TO FINANCIAL INSTITUTIONS AND CUSTOMERS

Group and Bank	2009 £	2008 £
Due to financial institutions - murabaha and wakala	365,959	2,374,638
Due to customers - murabaha and wakala	84,158	143,349
	<b>450,117</b>	<b>2,517,987</b>

## NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

### 6 FOREIGN EXCHANGE GAINS

	2009	2008
Group and Bank	£	£
Net (losses)/gains on translation of balances denominated in foreign currency	(1,303,106)	1,976,086
Net gains/(losses) on translation of forward foreign exchange agreements	1,394,446	(1,170,101)
	<b>91,340</b>	<b>805,985</b>

### 7 TRADING INCOME

	2009	2008
Group and Bank	£	£
Available for sale securities – Sukuk and equity securities	<b>309,813</b>	242,970

### 8 STAFF COSTS, DIRECTORS' EMOLUMENTS, NUMBER OF EMPLOYEES & SHARE BASED PAYMENTS

	2009	2008
	£	£
<b>Staff costs</b>		
Directors' salaries, fees and other	951,068	786,465
Directors' pension contributions (note 2.8.11)	37,330	27,475
Staff salaries	2,602,974	2,742,166
Staff pension contributions (note 2.8.11)	166,770	145,139
Share based payments to staff **	82,240	75,360
Incentive payments	200,055	364,000
Social security costs	411,986	353,958
Sharia'a Supervisory Board (SSB) fees	77,177	100,352
Recruitment costs	39,650	237,663
Other staff costs	140,472	183,481
	<b>4,709,722</b>	<b>5,016,059</b>
Included in SSB fees in respect of shares issued to SSB members *	-	4,444
<b>Total of Directors' emoluments</b>	<b>988,398</b>	<b>878,940</b>
Included in Directors' emoluments in respect of shares issued to Directors *	-	8,889
<b>Amounts in respect of highest paid Director</b>		
Emoluments	196,369	210,000
Compensation for loss of office	175,000	-
Pension contributions	16,150	23,100
	<b>387,519</b>	<b>233,100</b>
Number of employees at year end	34	39
Average number of employees	35	39

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 8 STAFF COSTS, DIRECTORS' EMOLUMENTS, NUMBER OF EMPLOYEES & SHARE BASED PAYMENTS continued

### 8.1 Share based payments

#### *\*Directors and SSB members share based payment scheme*

In February 2005, 12,000,000 ordinary 1p shares were issued to Directors and other staff at par in lieu of salaries for the 36 months from that point. They are deemed to have been issued at a premium of 7p per share under IFRS 2 Share-based payment. The fair value of the shares was amortised over the 36 month vesting period ended February 2008.

#### *\*\*Employee share incentive plan (ESIP)*

A part of the 2007 incentive (£112,000) was distributed during 2008 with 1,904,513 equity shares vesting in two equal instalments, in February 2009 and 2010. An equal amount of matching shares, were offered under the plan vesting in February 2010. These shares are valued at grant price (which is the market value at the date of grant) and the matching element is accrued in the financial statements on a time proportion basis. As a result a current year charge of £56,000 has been recognised (2008: £56,000).

#### *\*\*Employee share option plan (ESOP)*

An equity settled ESOP scheme was introduced in April 2008 with the aim of aligning the interests of executives with the creation of shareholder value. This is achieved by setting certain targets that have to be achieved for the awards to vest. The exercise price for the current plans is 7.7p and the options vest in March 2011, 2012 and 2013, a third in each year with a contractual life of 10 years from date of grant. The number of shares subject to the options granted during 2008 was 3,116,844. The options are valued using the Black-Scholes model. A current year charge of £26,240 is recognised (2008: £19,360).

The Bank has arranged an independent Trust to administer the ESIP and ESOP on behalf of employees and has provided funds to purchase a part of the current share obligation. The Trust is not consolidated given the value of the shares held is not material.

## 9 OTHER OPERATING EXPENSES

	2009	2008
	£	£
Legal and professional fees	944,789	583,625
Rent and other occupancy costs	502,186	459,043
Communications and IT costs	349,442	398,444
Advertising and market development	233,763	289,910
Consultancy	95,843	120,408
Board and SSB related expenses	133,578	105,998
Other operating charges	397,932	388,244
	<b>2,657,533</b>	<b>2,345,672</b>

## 10 OPERATING LOSS BEFORE TAX

This is stated after charging:	2009	2008
	£	£
Audit of group financial statements pursuant to legislation		
Auditors' remuneration:		
Statutory – group	165,000	273,030
Non-audit services	-	10,890
Rentals charge under operating leases	268,300	254,184

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 11 TAXATION

	2009	2008
	£	£
<b>Tax on profit on ordinary activities charged in the income statement</b>		
Current tax for the period	-	1,079,166
Adjustments to prior period tax		
- tax losses of 2008 carry back against 2007 profits	(986,580)	-
- tax credits accounted in equity transferred to income statement	(532,819)	-
- other prior year adjustments	-	(145,236)
<i>Current tax (income)/expense</i>	(1,519,399)	933,930
Deferred tax for the period	-	157,603
<b>Tax (credit)/charge in the income statement</b>	<b>(1,519,399)</b>	<b>1,091,533</b>
<b>Reconciliation of the total tax charge</b>		
Loss before tax	(23,698,714)	(13,721,590)
UK corporation tax at the standard rate (28%/ 28.5%)	(6,635,640)	(3,910,653)
Expenses not deductible for tax purposes	237,440	6,200,076
Income/expenses not subject to UK taxation	597,722	(1,052,655)
Adjustments to prior period tax	(986,580)	(145,235)
Effect of the tax losses carried forward **	5,267,659	-
<b>Tax (credit)/charge</b>	<b>(1,519,399)</b>	<b>1,091,533</b>
Current tax for the period	(986,580)	293,709
Current tax gain related to items charged to equity	-	(1,108,785)
Prior year's tax receivable	30,607	-
<b>Current tax receivable in the balance sheet</b>	<b>(955,973)</b>	<b>(815,076)</b>
Accelerated capital allowances	-	60,212
<b>Deferred tax liability in the balance sheet</b>	<b>-</b>	<b>60,212</b>

\*\* *Deferred tax asset on tax losses carried forward of £4.77m is not recognised in these financial statements given the current level of uncertainty surrounding the Bank's future taxable profits.*

As of 1 April 2008 the UK Corporation tax rate reduced to 28% from 30%. Tax asset and deferred tax liability have been computed at a rate of 28% (2008: 28%).

The 2008 loss before tax includes the results for discontinued operations.

## NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

### 12 EARNINGS PER SHARE

Basic earnings per share is calculated by dividing the loss for the year by the weighted average number of ordinary shares outstanding during the year. There are currently no instruments in issue which would materially dilute earnings per share.

	2009	2008
	'000	'000
Weighted average number of shares	1,822,280	1,825,562

### 13 DUE FROM FINANCIAL INSTITUTIONS

	2009	2008
Group and Bank	£	£
Murabaha placements	93,239,623	130,814,262
Wakala placements	27,056,351	13,551,630
	<b>120,295,974</b>	<b>144,365,892</b>

There are no due from financial institution facilities that are past due or impaired at 31 December 2009 and 2008.

### 14 FINANCING ARRANGEMENTS

	2009	2008
Group and Bank	£	£
<i>Murabaha</i>		
Central governments	-	6,878,998
Other counterparties	21,351,575	25,261,182
Impairment provision	(10,101,575)	(3,750,000)
	<b>11,250,000</b>	<b>28,390,180</b>

The impairment provision account balance as at 31 December 2009 consists of the brought forward balance from 2008 (£3.75m) and a new impairment provision made on a finance facility provided to a Middle Eastern based corporate. No other movements to the account have been recorded.

### 15 AVAILABLE FOR SALE SECURITIES

	2009	2008
Group and Bank	£	£
<i>Sukuk</i>		
Central governments	3,349,602	12,274,555
Financial institutions	5,323,535	7,163,548
Other counterparties	21,854,065	37,121,244
Impairment provision	(7,030,988)	-
	<b>23,496,214</b>	<b>56,559,347</b>

The impairment provision was raised against a Sukuk issued by a Middle Eastern corporate. No other movements have been recorded in the Sukuk impairment provision account during 2008 or 2009.

## NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

### 16 FINANCIAL ASSETS DESIGNATED AT FAIR VALUE

Group and Bank	2009 £	2008 £
<b>Private Equity investments</b>		
Opening book value	4,884,963	-
Additions	-	4,884,963
Fair value loss during the year	(4,134,525)	-
Closing book value	<b>750,438</b>	4,884,963

This private equity investment represents the Bank's acquisition of 26.1% of a public company during 2008. The Bank's shareholding diluted to 22.7% in 2009 when the investee company issued further shares for which the Bank did not subscribe. Investments are designated, upon initial recognition, at fair value through income statement and accounted for in accordance with IAS 39, with changes in fair value recognised in the income statement in the period of the change. Upon careful consideration of operational, financial and other indicators, the Management has decided to impair the asset from 45p per share to 7p per share, to reflect the potential reduction in the expected future cashflows from this investment.

### 17 FAIR VALUE OF FOREIGN EXCHANGE AGREEMENTS

Foreign exchange commitments used for matching currency exposures

Group and Bank	Assets £	Liabilities £	Notional amount £
<b>2009</b>			
Maturing in 0-3 months	30,091	539,811	40,785,453
Maturing in 3-6 months	-	-	-
	<b>30,091</b>	<b>539,811</b>	<b>40,785,453</b>
<b>2008</b>			
Maturing in 0-3 months	20,012	1,924,178	50,638,297
Maturing in 3-6 months	-	-	-
	20,012	1,924,178	50,638,297

### 18 PLANT AND EQUIPMENT

Group and Bank	Leasehold Improvements £	Fixtures, Fittings and office equipment £	Computer Hardware £	Total £
<b>Cost</b>				
At 1 January 2009	291,789	162,614	164,781	619,184
Additions	-	89	15,789	15,878
At 31 December 2009	<b>291,789</b>	<b>162,703</b>	<b>180,570</b>	<b>635,062</b>
<b>Depreciation</b>				
At 1 January 2009	115,690	72,125	138,262	326,077
Charge for the year	58,358	32,528	27,038	117,924
At 31 December 2009	<b>174,048</b>	<b>104,653</b>	<b>165,300</b>	<b>444,001</b>
<b>Net Book Value</b>				
At 31 December 2009	<b>117,741</b>	<b>58,050</b>	<b>15,270</b>	<b>191,061</b>

## NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

### 18 PLANT AND EQUIPMENT continued

Group and Bank	Leasehold Improvements £	Fixtures, Fittings and office equipment £	Computer Hardware £	Total £
<b>Cost</b>				
At 1 January 2008	275,412	152,397	164,293	592,102
Additions	16,377	10,217	1,884	28,478
Disposals	-	-	(1,396)	(1,396)
At 31 December 2008	291,789	162,614	164,781	619,184
<b>Depreciation</b>				
At 1 January 2008	58,315	39,937	84,525	182,777
Charge for the year	57,375	32,188	54,319	143,882
Disposals	-	-	(582)	(582)
At 31 December 2008	115,690	72,125	138,262	326,077
<b>Net Book Value</b>				
At 31 December 2008	176,099	90,489	26,519	293,107

### 19 INTANGIBLE ASSETS

Group and Bank	2009 £	2008 £
<b>Cost</b>		
At 1 January	1,436,343	1,384,587
Additions	19,923	51,756
At 31 December	<b>1,456,266</b>	1,436,343
<b>Amortisation</b>		
At 1 January	753,082	468,590
Charge for the year	287,672	284,492
At 31 December	<b>1,040,754</b>	753,082
<b>Net Book Value</b>		
At 31 December	<b>415,512</b>	683,261

Intangible assets consist of the costs of computer licences and software development including capitalised staff costs.

## NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

### 20 OTHER ASSETS

	2009	2008
Group	£	£
Accrued income receivable	72,117	1,400,438
Sundry debtors	346,767	436,258
Prepayments	653,478	138,521
Oil & gas other assets	675,109	-
	<b>1,747,471</b>	<b>1,975,217</b>

#### Bank

Accrued income receivable	72,117	1,155,455
Sundry debtors	346,767	221,044
Prepayments	653,478	138,521
	<b>1,072,362</b>	<b>1,515,020</b>

### 21 DUE TO FINANCIAL INSTITUTIONS

	2009	2008
Group	£	£
Commodity murabahas	18,175,937	88,733,239
Wakala acceptances	3,097,130	18,351,192
	<b>21,273,067</b>	<b>107,084,431</b>

#### Bank

Commodity murabahas	18,175,937	49,683,239
Wakala acceptances	3,097,130	18,351,192
	<b>21,273,067</b>	<b>68,034,431</b>

### 22 DUE TO CUSTOMERS

	2009	2008
Group and Bank	£	£
Wakala acceptances	1,009,533	2,728,522
	<b>1,009,533</b>	<b>2,728,522</b>

## NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

### 23 OTHER LIABILITIES

	2009	2008
Group	£	£
Accrued expenses	1,071,948	1,030,111
Accrued returns payable	7,482	630,740
Deferred income	248,017	321,600
Social security and PAYE payable	110,212	103,910
Sundry creditors	750,633	417,848
Oil & gas other liabilities	649,264	-
	<b>2,837,556</b>	<b>2,504,209</b>
<b>Bank</b>		
Accrued expenses	1,071,948	1,030,111
Accrued returns payable	7,482	93,008
Deferred income	248,017	321,600
Social security and PAYE payable	110,212	103,910
Sundry creditors	750,631	526,465
	<b>2,188,290</b>	<b>2,075,094</b>

### 24 MATURITY ANALYSIS OF ASSETS AND LIABILITIES

The tables below show an analysis of assets and liabilities analysed between those expected to be recovered or settled within or after more than twelve months of the balance sheet date.

2009 Group	Less than 12 months £	More than 12 months £	Total £
<b>Assets</b>			
Cash and balances with banks	685,495	-	685,495
Due from financial institutions	101,713,188	18,582,786	120,295,974
Financing arrangements	-	11,250,000	11,250,000
Available for sale securities – Sukuk	8,652,787	14,843,427	23,496,214
Available for sale securities – Equity	-	127,817	127,817
Financial assets designated at fair value	-	750,438	750,438
Fair value of foreign exchange agreements	30,091	-	30,091
Plant and equipment	-	191,061	191,061
Intangible assets	-	415,512	415,512
Oil & gas properties – intangible	-	6,162,050	6,162,050
Oil & gas properties – tangible	-	870,284	870,284
Other assets	1,747,471	-	1,747,471
Current tax	955,973	-	955,973
<b>Total assets</b>	<b>113,785,005</b>	<b>53,193,375</b>	<b>166,978,380</b>

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 24 MATURITY ANALYSIS OF ASSETS AND LIABILITIES continued

2009 Group	Less than 12 months £	More than 12 months £	Total £
<b>Liabilities</b>			
Due to financial institutions	21,273,067	-	21,273,067
Due to customers	1,009,533	-	1,009,533
Fair value of foreign exchange agreements	539,811	-	539,811
Other liabilities	2,243,983	593,573	2,837,556
<b>Total liabilities</b>	<b>25,066,394</b>	<b>593,573</b>	<b>25,659,967</b>

2008 Group	Less than 12 months £	More than 12 months £	Total £
<b>Assets</b>			
Cash and balances with banks	972,540	-	972,540
Due from financial institutions	123,728,897	20,636,995	144,365,892
Financing arrangements	17,140,180	11,250,000	28,390,180
Available for sale securities	25,775,734	30,783,613	56,559,347
Financial assets designated at fair value	-	4,884,963	4,884,963
Fair value of foreign exchange agreements	20,012	-	20,012
Property portfolio	-	38,699,245	38,699,245
Plant and equipment	-	293,107	293,107
Intangible assets	-	683,261	683,261
Other assets	1,975,217	-	1,975,217
Current tax	815,076	-	815,076
<b>Total assets</b>	<b>170,427,656</b>	<b>107,231,184</b>	<b>277,658,840</b>

<b>Liabilities</b>			
Due to financial institutions	68,034,431	39,050,000	107,084,431
Due to customers	2,728,522	-	2,728,522
Fair value of foreign exchange agreements	1,924,178	-	1,924,178
Other liabilities	2,504,209	-	2,504,209
Deferred taxation	-	60,212	60,212
<b>Total liabilities</b>	<b>75,191,340</b>	<b>39,110,212</b>	<b>114,301,552</b>

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 24 MATURITY ANALYSIS OF ASSETS AND LIABILITIES continued

2009	Less than 12 months	More than 12 months	Total
Bank	£	£	£
<b>Assets</b>			
Cash and balances with banks	459,065	-	459,065
Due from financial institutions	101,713,188	18,582,786	120,295,974
Financing arrangements	-	11,250,000	11,250,000
Available for sale securities - Sukuk	8,652,787	14,843,427	23,496,214
Available for sale securities - Equity	-	127,817	127,817
Financial assets designated at fair value	-	750,438	750,438
Investments in subsidiaries	-	6,345,002	6,345,002
Fair value of foreign exchange agreements	30,091	-	30,091
Plant and equipment	-	191,061	191,061
Intangible assets	-	415,512	415,512
Other assets	1,072,362	-	1,072,362
Current tax	955,973	-	955,973
<b>Total assets</b>	<b>112,883,466</b>	<b>52,506,043</b>	<b>165,389,509</b>

### Liabilities

Due to financial institutions	21,273,067	-	21,273,067
Due to customers	1,009,533	-	1,009,533
Fair value of foreign exchange agreements	539,811	-	539,811
Other liabilities	1,594,717	593,573	2,188,290
<b>Total liabilities</b>	<b>24,417,128</b>	<b>593,573</b>	<b>25,010,701</b>

2008	Less than 12 months	More than 12 months	Total
Bank	£	£	£
<b>Assets</b>			
Cash and balances with banks	652,867	-	652,867
Due from financial institutions	123,728,897	20,636,995	144,365,892
Financing arrangements	17,140,180	11,250,000	28,390,180
Available for sale securities	25,775,734	30,783,613	56,559,347
Financial assets designated at fair value	-	4,884,963	4,884,963
Fair value of foreign exchange agreements	20,012	-	20,012
Plant and equipment	-	293,107	293,107
Intangible assets	-	683,261	683,261
Other assets	1,515,020	-	1,515,020
Current tax	815,076	-	815,076
<b>Total assets</b>	<b>169,647,786</b>	<b>68,531,939</b>	<b>238,179,725</b>

## NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

### 24 MATURITY ANALYSIS OF ASSETS AND LIABILITIES continued

2008	Less than 12 months	More than 12 months	Total
Bank	£	£	£
<b>Liabilities</b>			
Due to financial institutions	68,034,431	-	68,034,431
Due to customers	2,728,522	-	2,728,522
Fair value of foreign exchange agreements	1,924,178	-	1,924,178
Other liabilities	2,075,094	-	2,075,094
Deferred taxation	-	60,212	60,212
<b>Total liabilities</b>	<b>74,762,225</b>	<b>60,212</b>	<b>74,822,437</b>

### 25 PENSION COMMITMENTS

The Bank provides a defined contribution scheme for all staff. The assets of the scheme are held separately from those of the Bank in independently administered funds. Total costs of 2009 and 2008 are fully settled by each year end.

### 26 COMMITMENTS UNDER OPERATING LEASES

There is a commitment at the year end under a non-cancellable operating lease for the Bank's main premises at 4th Floor, 131 Finsbury Pavement, London EC2A 1NT for a five-year period from 27 December 2005 to 27 December 2010, at an annual rental of £267,498 net of VAT with a fifteen-month rent free period. In addition, there is an agreement under an operating lease for the Bank's premises in Bahrain at an annual rental of BHD 37,059 for a 5 year period from 15 May 2007 to 14 May 2012. For the first three years to 14 May 2010 the lease is irrevocable with rent renewals on a semi-annual basis. Future rentals are as follows:

	2009	2008
	£	£
<b>Group and Bank</b>		
Within one year	259,758	261,515
One to five years	83,413	345,095
More than five years	-	-
	<b>343,171</b>	<b>606,610</b>

### 27 CONTINGENT LIABILITIES AND COMMITMENTS

No contingent liabilities or contractually obligatory commitments outstanding as at the balance sheet date and up to the date that these financial statements were approved other than the operating lease obligations (above).

## NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

### 28 SHARE CAPITAL, SHARE PREMIUM AND CAPITAL REDEMPTION RESERVE

Authorised	£			
5,000,000,000 ordinary shares of £0.01 each				50,000,000
	Number of shares	Share capital £	Capital Redemption Reserve £	Share Premium £
<b>Allotted, called up and fully paid</b>				
At 31 December 2009	1,765,658,553	17,656,585	599,040	116,219,800
At 31 December 2008	1,825,562,531	18,255,625	-	164,229,939

In December 2009, the Bank concluded a capital reduction and tender offer whereby it purchased (through Evolution Securities, its Nominated Adviser and Broker) and cancelled 59,903,978 of its own shares. This involved a Court approved reduction of the Bank's share premium account amounting to £48,010,139 and transfer of the amount to a special reserve. The special reserve was utilised to fund the share redemption and the balance to extinguish the Bank's negative retained earnings. The terms of the capital reduction and tender offer are contained in a circular that was sent to shareholders on 28 October 2009 and which is available on the Bank's website at [www.eiib.co.uk](http://www.eiib.co.uk).

The capital reduction and tender offer were approved by shareholders by special resolution at a General Meeting held on 13 November 2009.

### 29 ASSETS AND LIABILITIES IN FOREIGN CURRENCY

The Bank manages its exposure to foreign exchange rate fluctuations by matching assets with liabilities in the same currency as far as possible, with similar maturities and the use of appropriate off-balance sheet instruments.

Group	2009 £	2008 £
Denominated in sterling	110,402,613	165,177,648
Denominated in currencies other than sterling	56,575,767	112,481,192
<b>Total assets</b>	<b>166,978,380</b>	<b>277,658,840</b>
Denominated in sterling	6,736,949	50,394,193
Denominated in currencies other than sterling	18,923,018	63,907,359
<b>Total liabilities</b>	<b>25,659,967</b>	<b>114,301,552</b>

Bank	2009 £	2008 £
Denominated in sterling	110,402,613	125,698,533
Denominated in currencies other than sterling	54,986,896	112,481,192
<b>Total assets</b>	<b>165,389,509</b>	<b>238,179,725</b>
Denominated in sterling	6,736,948	10,915,078
Denominated in currencies other than sterling	18,273,753	63,907,359
<b>Total liabilities</b>	<b>25,010,701</b>	<b>74,822,437</b>

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 30 INVESTMENTS IN SUBSIDIARIES

The Bank's subsidiaries as at 31 December 2009 are as follows:

Company	Principal Activity	Control %	Country of registration
EIIB InvestCo SPC *	Limited partner	100	Bahrain
EIIB ServiceCo WLL *	General partner	100	Bahrain
TriTech Capital Limited	Oil & gas exploration	87	British Virgin Islands

\* no business activities during 2009

The Bank's controlled entities as at 31 December 2008 were as follows:

EIIB Pan-European Islamic Real Estate Fund**	Holding company	100	Cayman Islands
The House Limited**	Real Estate	100	Cayman Islands

\*\* disposed of in 2009

	2009
<b>Investment in subsidiaries</b>	<b>£</b>
At 1 January	-
Additions	8,153,134
Fair value loss during the year	(1,808,132)
<b>At 31 December</b>	<b>6,345,002</b>

There was no movement in 2008.

### 30.1 Acquisition of a subsidiary

On 20 March 2009, as part of EIIB's Private Equity and Corporate Advisory activities, the Group obtained control of TriTech Capital Ltd (BVI) (and the entities incorporated as its subsidiaries, together the 'TriTech Capital Group'). Control was obtained by acquiring a shareholding in TriTech Capital Ltd (BVI) and entering into a shareholders' agreement that enables the Bank to appoint the majority of the directors to the board of the TriTech Capital Group companies.

The investment was structured via a financing facility with rights to convert the facility into equity shares at any time as determined by EIIB. EIIB's interest in TriTech for consolidation purposes is determined based on its effective interest in the net assets of the investee.

Identifiable assets and liabilities of TriTech Capital Group as at the date of acquisition:

	£
Cash & bank balances	810,512
Oil & Gas assets	7,583,539
Other assets	252,938
Other liabilities	(496,605)
Net assets	8,150,384
Non controlling interest (13.1322%)	(1,070,326)
Total net assets acquired	7,080,058
Goodwill	954,077
Consideration satisfied by cash	8,034,135

There were no significant differences between carrying values and fair values at the date of acquisition.

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 30 INVESTMENTS IN SUBSIDIARIES continued

<b>Goodwill:</b>	<b>£</b>
Total consideration transferred in respect of financing facility and equity share (all settled in cash)	8,034,135
Less: value of identifiable net assets	(7,080,058)
Goodwill on acquisition	954,077
Impairment	(954,077)
<b>Balance</b>	<b>-</b>

Goodwill was created on acquisition as the cost exceeded EIB's interest in the fair values of TriTech's identified net assets. The goodwill was impairment tested as at 31 December 2009 in compliance with IAS 36, evaluating the results so far and the possible outcomes. In line with the Board's cautious approach on asset valuation, management has decided to impair the goodwill.

### The effective interest of EIB and that of the Non-controlling interest:

The following table illustrates the effective interest of EIB and that of the non-controlling equity contributors based on the IAS 27 which states that the proportion allocated is determined taking into account the eventual exercise of potential voting rights. Accordingly the financing facility is treated as an equity stake for consolidation purposes and to calculate the effective non-controlling interest.

	Date	% acquired by EIB	EIB cumulative %	Non-controlling interest %
Initial drawdown of facility	20 Mar 09	82.58%	82.58%	17.42%
Second drawdown of facility	12 May 09	2.58%	85.16%	14.84%
Third drawdown of facility	11 Jun 09	1.70%	86.87%	13.13%

Had the acquisition date been 1 January 2009, the Group would have made a post-tax loss of £22.5m on its continuing operations. The Group's total revenue would have been unchanged.

The investment in the TriTech project is the second investment made by the business segment, 'Private Equity and Corporate Advisory' after its establishment in 2008.

### 30.2 Oil and gas properties

Oil and gas properties capitalised during the year are as follows. All these assets were acquired by the Group during the year as a part of the acquisition of TriTech Capital Group.

	<b>2009</b>
	<b>£</b>
<b>Unproved intangible mineral interest</b>	
- Intangible drilling	2,426,991
- Intangible completion	1,075,590
- Prospect development	2,801
- Leasehold costs	2,656,517
	<b>6,161,899</b>

## NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

### 30 INVESTMENTS IN SUBSIDIARIES continued

	2009
	£
<b>Unproved property, plant &amp; equipment</b>	
- Tangible	639,472
- Facilities	196,895
- Buildings	1,053
- Leasehold improvements	14,353
- Inventory	18,662
	<b>870,435</b>
<b>Total oil and gas properties</b>	<b>7,032,334</b>

In accordance with IFRS 6 and the accounting policy stated in note 2.7.3 above, all oil & gas exploration costs are capitalised as intangible assets on acquisition. These are tested for impairment on a regular basis, based on the results of exploratory activity and management's evaluation thereof. No impairment allowances have been made against the oil & gas properties during the year.

### 31 INVESTMENT PROPERTY

The Bank's interest in the asset management special purpose vehicle, EIBB Pan-European Islamic Real Estate Fund (the Fund), which held a UK commercial real estate property portfolio through its investment in The House Limited (THL) was sold to a third party in December 2009 for negligible consideration.

The Fund was established on 22 November 2006, and the property portfolio was acquired on 18 April 2007. The acquisition of the properties was financed by a third-party financial institution on a murabaha basis and the Bank via a bridging facility. The Bank owned 100% of the management shares in the Fund, there being no other equity shares in issue. In turn the Fund owned 100% of the equity shares of THL, the company which owns the properties. Both the Fund and THL are registered in the Cayman Islands. As a result of the nature of the relationship between the Bank and the Fund, the requirements of IAS 27 and Standard Interpretation Committee (SIC) 12, the results of the Fund and the underlying property portfolio were consolidated with those of the Bank in 2008.

Following a breach of a covenant in 2008 the third-party financial institution appointed an administrator to take over all the properties of THL. The property activities were accounted for under IFRS 5 "Discontinued operations" in the Bank's interim financial statements as at 30 June 2009. The fund was sold in December 2009 and was therefore deconsolidated as at 31 December 2009. The Group's reported loss on THL activities of £7.1m in its June 2009 interim financial statements has therefore been offset by an equivalent profit arising following the disposal of the Fund.

The Bank's consolidated statement of financial position for 2008 recognised the properties in accordance with the requirements of IAS 40. Accordingly these properties were carried at original cost less depreciation and were impairment tested for reporting purposes. The Group estimated the recoverable amount for this purpose. The recoverable amount of an asset is the higher of its fair value less cost to sell, and its value in use. Value in use is the present value of future cash flows from the assets discounted at a rate that reflects market returns adjusted for risks specific to the assets. When the recoverable amount of an asset is less than its carrying value, an impairment loss is recognised immediately in profit or loss and the carrying value of the asset reduced by the amount of the loss. The value in use of the property portfolio as at 31 December 2008 was £38,699,245.

As the Bank had provided junior financing to THL via the Fund, an impairment provision of £14,285,451 was charged against the income statement in 2008. The following items in the income statement and balance sheet relate to the Fund and THL:

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 31 INVESTMENT PROPERTY continued

	2009	2008
	£	£
Rental income	1,991,000	3,693,527
Returns related to the property portfolio *	(1,779,000)	(2,555,972)
Foreign exchange gains and losses	-	-
Operating expenses of the property portfolio	(212,000)	(423,006)
Depreciation	-	(294,086)
Provision for impairment of the property portfolio	(7,084,020)	(14,705,914)
Disposal of property portfolio	7,084,020	-
<b>Total loss relating to the property portfolio</b>	<b>-</b>	<b>(14,285,451)</b>

\* Murabaha returns on due to financial institutions.

	2009	2008
	£	£
Balance brought forward	38,699,245	53,699,245
Depreciation	-	(294,086)
Provision for impairment	-	(14,705,914)
Disposal of property portfolio	(38,699,245)	-
<b>Balance carried forward</b>	<b>-</b>	<b>38,699,245</b>

## 32 RELATED PARTY DISCLOSURES

### 32.1 Compensation of key management personnel

	2009	2008
	£	£
Short-term employee benefits and other cash payments	776,068	740,076
Incentive payment	-	15,000
Termination benefits	175,000	87,500
Post-employment pension	37,330	27,475
Share-based payments	-	8,889
	<b>988,398</b>	<b>878,940</b>

### 32.2 Other Directors' interests

The Bank enters into transactions, arrangements and agreements involving Directors and their related concerns in the ordinary course of business. All such business is conducted on an arm's length basis.

Mr. Adnan Ahmed Yousif the Chairman of EIIB is the President and the Chief Executive of the AlBaraka Group with whom EIIB has had business dealings during 2009. Subhi Benkhadra, a Director of EIIB has been the Chief Executive of Esterad Investment Company BSC ('Esterad') during 2009, with whom EIIB has conducted murabaha transactions during 2009.

Total returns to related parties (companies and individuals) were £44,881 during 2009 (2008: £691,341) and this is included under *Returns to financial institutions and customers*. There is no income earned from related parties during the year (2008: £830,686). Further, no amounts were outstanding as at 31 December 2009 (2008: wakala acceptance liabilities to Esterad and Mr Adnan Ahmed Yousif of £7,566,898 and £1,354,709 respectively).

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 33 VALUATION OF FINANCIAL INSTRUMENTS

The Group's accounting policy on fair value measurements is discussed in note 2.7.1 above.

The Group measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

*Level 1: Quoted market price (unadjusted) in an active market for an identical instrument*

*Level 2: Valuation techniques based on observable inputs, either directly (i.e. as prices) or indirectly (i.e. derived from prices)*

This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data.

*Level 3: Valuation techniques using significant unobservable inputs*

This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

Fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments the Group determines fair values using valuation techniques.

Valuation techniques include net present value and discounted cash flow models, comparison to similar instruments for which market observable prices exist and other valuation models. Assumptions and inputs used in valuation techniques include risk-free and benchmark rate of returns, credit spreads and other premia used in estimating discount rates, bond and equity prices, foreign currency exchange rates and net asset valuations. The objective of valuation techniques is to arrive at a fair value determination that reflects the price of the financial instrument at the reporting date that would have been determined by market participants acting at arm's length.

The Group has an established control framework with respect to the measurement of fair values. This framework includes an independent price verification activity and the risk division report to the Chief Executive Officer, and the Group's Risk and Audit committees. The division has overall responsibility for independently verifying the transactions, assets and all significant fair value measurements.

The table below analyses financial instruments measured at fair value at the end of the reporting period, by the level in the fair value hierarchy into which the fair value measurement is categorised

Bank	Level 1	Level 2	Level 3	Total
At 31 December 2009	£	£	£	£
<b>Assets</b>				
Available for sale securities – Sukuk	-	17,997,993	5,498,221	23,496,214
Available for sale securities – Equity	127,817	-	-	127,817
Financial assets designated at fair value	-	-	750,438	750,438
Investments in subsidiaries*	-	119,000	6,226,002	6,345,002
Fair value of foreign currency arrangements	-	30,091	-	30,091
	<b>127,817</b>	<b>18,147,084</b>	<b>12,474,661</b>	<b>30,749,562</b>
<b>Liabilities</b>				
Fair value of foreign currency arrangements	-	539,811	-	539,811
	-	<b>539,811</b>	-	<b>539,811</b>

## NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

### 33 VALUATION OF FINANCIAL INSTRUMENTS continued

The following table reconciles the opening balances to the closing balances for fair value measurements in Level 3 of the fair value hierarchy.

2009	Available for sale securities – Sukuk	Financial assets designated at fair value	Investments in subsidiaries*	Total
Balance at 1 January	6,406,735	4,884,963	-	11,291,698
Purchases	-	-	8,034,134	8,034,134
Total gains or losses:	(424,589)	(4,134,525)	(1,808,132)	(6,367,246)
- in income statement	-	(4,134,525)	(1,808,132)	(5,942,657)
- in other comprehensive income	(424,589)	-	-	(424,589)
Settlements	(483,925)	-	-	(483,925)
<b>Balance at 31 December</b>	<b>5,498,221</b>	<b>750,438</b>	<b>6,226,002</b>	<b>12,474,661</b>

\* The above tables reflect the Bank only position. For the Group position the 'Investments in subsidiaries' should be removed.

Although the Group believes that its estimates of fair value are appropriate, the use of different methodologies or assumptions could lead to different measures of fair value. For fair value measurements in Level 3, changing one or more of the assumptions used to reasonably possible alternative assumptions would have the following effects:

31 December 2009	Effect on profit or loss		Effect on comprehensive income	
	Favourable £	(Unfavourable) £	Favourable £	(Unfavourable) £
Available for sale securities - Sukuk	-	-	145,178	(145,178)
Financial Assets designated at fair value	214,411	(214,411)	-	-
Investments in subsidiaries	-	(6,226,002)	-	-
	<b>214,411</b>	<b>(6,440,413)</b>	<b>145,178</b>	<b>(145,178)</b>

### 34 RISK MANAGEMENT

#### 34.1 Introduction

The Board of Directors have set an overall risk framework in line with risk appetite, documented within a set of risk management policies which are approved by mandated risk committees. Ultimate responsibility for risk resides with the Board of Directors.

The Bank is exposed mainly to credit risk, liquidity risk, market risk and operational risk.

#### 1 Structure

The Board of Directors is ultimately responsible for managing the risk profile of the Bank and ensuring a strong control environment. The Board has mandated a number of committees tasked with managing and monitoring risks within the Bank.

#### a Board of Directors

The Board of Directors is responsible for the overall risk management approach and for approving the risk appetite, tolerances, strategies and principles.

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 34 RISK MANAGEMENT continued

### *b Board Executive Committee*

The Board Executive Committee is a sub-committee of the Board of Directors which assists the Board in fulfilling its risk management responsibilities from day to day. The committee's responsibilities includes determining the Bank's risk profile, ensuring that exposures taken on by management remain within the Board determined risk appetite by assessing, reviewing, and approving all exposures that are within its delegated authority.

### *c Risk Management Committee*

The Risk Management Committee assists the Executive Management Committee and the Board of Directors in managing and controlling risk in all areas of the Bank, through proactive identification, measurement, control, monitoring, and reporting of:

- Credit risk
- Market risk
- Liquidity risk
- Operational risk including other residual risks

### *d Asset and Liability Committee*

The Asset and Liability Committee ('ALCO') is constituted to assist the Executive Management Committee and the Board in proactively managing the capital, assets and liabilities of the Bank. It is also mandated to manage the risk-reward relationship that exists between solvency, liquidity and profit rate risk.

### *e Internal Audit*

Internal Audit's primary role is to provide assurance to the Audit Committee and the Board that the risk management, internal control, corporate governance and other key business processes and controls, as appropriate, are operating effectively and meeting the ongoing and changing needs of the Bank. This includes providing management with independent appraisals of systems of internal control and supporting development of a sound control culture throughout the Bank.

## 2 Measurement and reporting

The risks within the Bank are assessed using quantitative and qualitative methodologies. Losses are calculated using assumptions based on consideration of the economic environment in which the Bank operates, stress scenarios and conditions in the Islamic banking market.

Risk is managed by a set of comprehensive limits, triggers and processes. These reflect the business strategy, risk appetite and market environment in which the Bank operates and its overall risk capacity in relation to capital and regulatory requirements set by the UK Financial Services Authority.

Information is compiled by the Risk Management department from all business areas and is then presented to the Executive Management Committee and Board on a monthly basis. The Risk Report includes detailed reporting of credit exposures for internal ratings, geographical regions, industry sectors, asset maturities, liquidity, and market risk exposures for foreign exchange, money and capital market instruments.

Daily reports on credit exposure and position risk are compiled and distributed by the Risk Management department to senior management.

## 3 Risk mitigation

Risk mitigants are used where possible. However the Bank cannot use conventional derivative products to mitigate risk. Consequently as part of its overall risk management framework the Bank utilises Sharia'a compliant products to hedge currency risk and profit rate risk.

## 4 Concentration risk

Concentration risk arises when a number of counterparties are engaged in similar business activities, or activities in the same geographic regions, or have similar economic characteristics that would cause their ability to meet contractual obligations to be similarly affected by a change in economic, political or other conditions.

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 34 RISK MANAGEMENT continued

In order to avoid excessive concentration risk the Bank has specific guidelines and limits in place to restrict Group, Obligor, Country and Industry sector exposures.

### 34.2 Credit risk

Credit risk is the risk that the Bank's customers, clients or counterparties will not be able or willing to repay capital and/or profit or otherwise not meet their contractual obligations under credit facilities or in respect of other agreements.

The Bank has a rigorous credit approval process for all customers, clients and counterparties and all are assigned an internal risk rating. Exposures are subject to regular review.

#### 1 Exposure

	2009 Group	2009 Bank	2008 Group	2008 Bank
Exposures by asset class were:	£	£	£	£
<b>Assets carried at amortised cost</b>				
Cash and balances with banks	685,495	459,065	972,540	972,540
Due from financial institutions	120,355,650	120,355,650	144,651,139	144,651,139
- <i>Wakala</i>	27,057,596	27,057,596	13,552,012	13,552,012
- <i>Murabaha</i>	93,298,054	93,298,054	131,099,127	131,099,127
Financing arrangements	11,287,178	11,287,178	28,717,677	28,717,677
Investments in oil and gas	7,032,334	-	-	-
<b>Assets carried at fair value</b>				
Available for sale securities				
- Sukuk	23,567,314	23,567,314	57,102,057	57,102,057
- Equity	127,817	127,817	-	-
<b>Fair value through income statement</b>				
Financial assets designated at fair value	750,438	750,438	4,884,963	4,884,963
Fair value of foreign exchange agreements	30,091	30,091	20,012	20,012
Investments property	-	-	38,699,245	-
Investments in subsidiaries	-	6,345,002	-	-
<b>Total credit exposure</b>	<b>163,836,317</b>	<b>162,922,555</b>	<b>275,047,633</b>	<b>236,348,388</b>

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 34 RISK MANAGEMENT continued

### 2 Geographical regions

	2009 Group	2009 Bank	2008 Group	2008 Bank
Exposures by geographical region were:	£	£	£	£
GCC countries	82,603,660	82,603,660	133,050,083	133,050,083
<i>Bahrain</i>	45,039,942	45,039,942	57,555,161	57,555,161
<i>UAE</i>	25,616,232	25,616,232	40,950,257	40,950,257
<i>Kuwait</i>	-	-	4,079,000	4,079,000
<i>Saudi Arabia</i>	8,413,347	8,413,347	26,358,878	26,358,878
<i>Qatar</i>	3,534,139	3,534,139	4,106,787	4,106,787
Europe	71,341,710	71,341,710	129,275,142	90,575,897
USA	7,139,764	6,226,002	-	-
Turkey	-	-	1,168,095	1,168,095
Asia	2,000,745	2,000,745	6,669,350	6,669,350
Africa	750,438	750,438	4,884,963	4,884,963
<b>Total credit exposure</b>	<b>163,836,317</b>	<b>162,922,555</b>	<b>275,047,633</b>	<b>236,348,388</b>

### 3 Industry Sector

	2009 Group	2009 Bank	2008 Group	2008 Bank
Exposures by industry sector were:	£	£	£	£
Financial services	126,403,157	126,295,727	152,862,752	152,862,752
<i>GCC banks</i>	64,121,671	64,121,671	73,372,388	73,372,388
<i>Europe/Other banks</i>	62,281,486	62,174,056	79,490,364	79,490,364
Manufacturing	11,415,216	11,415,216	25,443,431	25,443,431
Government	5,909,397	5,909,397	19,288,320	19,288,320
Real estate	12,325,775	12,325,775	69,321,373	30,622,128
Other financial	-	-	2,078,699	2,078,699
Mining	7,782,772	6,976,440	4,884,963	4,884,963
Food	-	-	1,168,095	1,168,095
<b>Total credit exposure</b>	<b>163,836,317</b>	<b>162,922,555</b>	<b>275,047,633</b>	<b>236,348,388</b>

### 4 Credit quality

The credit quality of exposures is continuously monitored. Internal credit ratings are mapped to ECAI ratings including Fitch, Moody's and Standard & Poor's. The table below shows the credit quality of the portfolio as at 31 December 2009 based on the Bank's credit rating system.

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 34 RISK MANAGEMENT continued

	Investment Grade	Non-Investment Grade	Total
2009 Group	£	£	£
Cash and balances with banks	685,495	-	685,495
Private Equity Investments	-	750,438	750,438
Due from Financial Institutions	85,379,403	34,976,247	120,355,650
Financing arrangements	-	11,287,178	11,287,178
Available for sale securities – Sukuk	13,728,008	9,839,306	23,567,314
Available for sale securities – Equity	127,817	-	127,817
Investment in oil and gas exploration	-	7,032,334	7,032,334
Fair value of foreign exchange agreements	30,091	-	30,091
<b>Total credit exposure</b>	<b>99,950,814</b>	<b>63,885,502</b>	<b>163,836,317</b>

### 2009 Bank

Cash and balances with banks	459,065	-	459,065
Private Equity Investments	-	750,438	750,438
Due from Financial Institutions	85,379,403	34,976,247	120,355,650
Financing arrangements	-	11,287,178	11,287,178
Available for sale securities – Sukuk	13,728,008	9,839,306	23,567,314
Available for sale securities – Equity	127,817	-	127,817
Investment in subsidiaries	-	6,345,002	6,345,002
Fair value of foreign exchange agreements	30,091	-	30,091
<b>Total credit exposure</b>	<b>99,724,384</b>	<b>63,198,171</b>	<b>162,922,555</b>

	Investment Grade	Non-Investment Grade	Total
2008 Group	£	£	£
Cash and balances with banks	972,540	-	972,540
Private Equity Investments	-	4,884,963	4,884,963
Due from Financial Institutions	119,287,515	4,502,641	123,790,156
Financing arrangements	27,812,052	21,766,608	49,578,660
Available for sale securities	40,912,392	16,189,665	57,102,057
Fair value of foreign exchange agreements	20,012	-	20,012
Investment property	38,699,245	-	38,699,245
<b>Total credit exposure</b>	<b>227,703,756</b>	<b>47,343,877</b>	<b>275,047,633</b>

## NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

### 34 RISK MANAGEMENT continued

	Investment Grade	Non-Investment Grade	Total
2008 Bank	£	£	£
Cash and balances with banks	972,540	-	972,540
Private Equity Investments	-	4,884,963	4,884,963
Due from Financial Institutions	119,287,515	4,502,641	123,790,156
Financing arrangements	27,812,052	21,766,608	49,578,660
Available for sale securities	40,912,392	16,189,665	57,102,057
Fair value of foreign exchange agreements	20,012	-	20,012
<b>Total credit exposure</b>	<b>189,004,511</b>	<b>47,343,877</b>	<b>236,348,388</b>

### 5 Aged analysis of past due and impaired financial assets

As at 31 December 2009 the Group has decided to maintain the 25% impairment allowance (£3.75m) it made during 2008, on a financing arrangement. This facility is classified as 'Sub-standard'. The new impairment provisions for 2009 relate to: (a) two assets comprising gross exposures of £14.4m (Financing arrangement of £6.4m and Sukuk of £8m) on which a total impairment provision of £13.4m (£6.4m on Financing arrangement and £7.0m on Sukuk) is charged, both classified as 'in-default' and 'impaired' – these have been in-default since August 2009 and November 2009 respectively; and, (b) a fair value loss of £4.1m on a private equity asset and an impairment loss of £0.9m on the goodwill which arose on acquisition of an oil and gas investment.

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 34 RISK MANAGEMENT continued

### 34.3 Liquidity risk

Liquidity risk is the risk that the Bank will be unable to meet its payment obligations when they fall due. To limit this risk the Bank manages the maturities of its assets and liabilities and its cash flows on a daily basis and maintains a portfolio of short-term bank deposits. Liquidity risk management is the responsibility of ALCO.

#### 34.3.1 Liquidity profile

Liquidity is managed based on contractual cash flows. The Group and Bank had the following liquidity profiles which include forward foreign exchange commitments:

Foreign currency amounts in sterling equivalents

2009 Liquidity profile (£000) Group	Cash flow band						
	Total	0-1 month	2-3 months	4-6 months	7-12 months	1-5 years	Over 5 years
<b>GBP</b>							
Assets	151,187	136,545	1,956	30	-	11,906	750
Liabilities	6,733	3,000	3,733	-	-	-	-
<b>Net</b>	<b>144,454</b>	<b>133,545</b>	<b>(1,777)</b>	<b>30</b>	<b>-</b>	<b>11,906</b>	<b>750</b>
<b>USD</b>							
Assets	55,618	6,387	6,018	-	1,048	31,864	10,301
Liabilities	59,576	59,576	-	-	-	-	-
<b>Net</b>	<b>(3,958)</b>	<b>(53,189)</b>	<b>6,018</b>	<b>-</b>	<b>1,048</b>	<b>31,864</b>	<b>10,301</b>
<b>Euro</b>							
Assets	12	12	-	-	-	-	-
Liabilities	-	-	-	-	-	-	-
<b>Net</b>	<b>12</b>	<b>12</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>BHD</b>							
Assets	135	16	-	-	-	-	119
Liabilities	-	-	-	-	-	-	-
<b>Net</b>	<b>135</b>	<b>16</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>119</b>
<b>AED</b>							
Assets	919	-	-	-	-	791	128
Liabilities	-	-	-	-	-	-	-
<b>Net</b>	<b>919</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>791</b>	<b>128</b>
<b>Total</b>							
Assets	207,871	142,960	7,974	30	1,048	44,561	11,298
Liabilities	66,309	62,576	3,733	-	-	-	-
<b>Net</b>	<b>141,562</b>	<b>80,384</b>	<b>4,241</b>	<b>30</b>	<b>1,048</b>	<b>44,561</b>	<b>11,298</b>

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 34 RISK MANAGEMENT continued

2009	Cash flow band						
Liquidity profile (€000)		0-1	2-3	4-6	7-12	1-5	Over 5
Bank	Total	month	months	months	months	years	years
<b>GBP</b>							
Assets	151,187	136,545	1,956	30	-	11,906	750
Liabilities	6,733	3,000	3,733	-	-	-	-
<b>Net</b>	<b>144,454</b>	<b>133,545</b>	<b>(1,777)</b>	<b>30</b>	<b>-</b>	<b>11,906</b>	<b>750</b>
<b>USD</b>							
Assets	53,922	6,280	6,018	-	1,048	31,864	8,712
Liabilities	59,576	59,576	-	-	-	-	-
<b>Net</b>	<b>(5,654)</b>	<b>(53,296)</b>	<b>6,018</b>	<b>-</b>	<b>1,048</b>	<b>31,864</b>	<b>8,712</b>
<b>Euro</b>							
Assets	12	12	-	-	-	-	-
Liabilities	-	-	-	-	-	-	-
<b>Net</b>	<b>12</b>	<b>12</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>BHD</b>							
Assets	135	16	-	-	-	-	119
Liabilities	-	-	-	-	-	-	-
<b>Net</b>	<b>135</b>	<b>16</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>119</b>
<b>AED</b>							
Assets	919	-	-	-	-	791	128
Liabilities	-	-	-	-	-	-	-
<b>Net</b>	<b>919</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>791</b>	<b>128</b>
<b>Total</b>							
Assets	206,175	142,853	7,974	30	1,048	44,561	9,709
Liabilities	66,309	62,576	3,733	-	-	-	-
<b>Net</b>	<b>139,866</b>	<b>80,277</b>	<b>4,241</b>	<b>30</b>	<b>1,048</b>	<b>44,561</b>	<b>9,709</b>

# NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

## 34 RISK MANAGEMENT continued

2008	Cash flow band						
Liquidity profile (£000)		0-1	2-3	4-6	7-12	1-5	Over 5
Group	Total	months	months	months	months	years	years
<b>GBP</b>							
Assets	212,822	134,238	20,000	-	-	19,885	38,699
Liabilities	46,229	4,903	621	1,555	100	39,050	-
Net	166,593	129,335	19,379	(1,555)	(100)	(19,165)	38,699
<b>USD</b>							
Assets	111,362	17,026	6,796	6,879	29,348	48,320	2,993
Liabilities	116,127	116,127	-	-	-	-	-
Net	(4,765)	(99,101)	6,796	6,879	29,348	48,320	2,993
<b>Euro</b>							
Assets	7	7	-	-	-	-	-
Liabilities	-	-	-	-	-	-	-
Net	7	7	-	-	-	-	-
<b>Total</b>							
Assets	324,190	151,270	26,796	6,879	29,348	68,205	41,692
Liabilities	162,356	121,030	621	1,555	100	39,050	-
Net	161,834	30,240	26,175	5,324	29,248	29,155	41,692

2008	Cash flow band						
Liquidity profile (£000)		0-1	2-3	4-6	7-12	1-5	Over 5
Bank	Total	month	months	months	months	years	years
<b>GBP</b>							
Assets	174,123	134,238	20,000	-	-	19,885	-
Liabilities	7,179	4,903	621	1,555	100	-	-
Net	166,944	129,335	19,379	(1,555)	(100)	19,885	-
<b>USD</b>							
Assets	111,362	17,026	6,796	6,879	29,348	48,320	2,993
Liabilities	116,127	116,127	-	-	-	-	-
Net	(4,765)	(99,101)	6,796	6,879	29,348	48,320	2,993
<b>Euro</b>							
Assets	7	7	-	-	-	-	-
Liabilities	-	-	-	-	-	-	-
Net	7	7	-	-	-	-	-
<b>Total</b>							
Assets	285,492	151,271	26,796	6,879	29,348	68,205	2,993
Liabilities	123,306	121,030	621	1,555	100	-	-
Net	162,186	30,241	26,175	5,324	29,248	68,205	2,993

## NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

### 34 RISK MANAGEMENT continued

As at 31 December 2009 and at 31 December 2008, the Bank had no contingent liabilities or other commitments outstanding in financial instruments other than those included above or in note 26.

#### 34.3.2 Liquidity ratios

The Bank manages its liquidity within the Financial Services Authority's prudential limits of 0% for 8 days and under and -5% 1 month and under. The ratios at the year end were:

	8 days and under	1 month and under
31 December 2009	159%	361%
31 December 2008	20%	48%

#### 34.4 Market risk – non-trading

##### 1 Profit Rate Risk

Profit rate risk arises from the possibility that changes in the profit rates will affect future cash flows. The Bank manages profit rate risk by using maturity buckets to calculate the net profit rate gap whilst considering variable, fixed and non-sensitive rates of return.

2009 Profit Rate profile (€000) Group	Total	Rate profile band					
		0-1 month	2-3 months	4-6 months	7-12 months	1-5 years	Over 5 years
<b>Assets</b>							
Fixed Rate Items	103,450	101,713	-	-	-	1,737	-
Variable Rate Items	51,591	18,556	14,594	18,441	-	-	-
Non rate Sensitive	8,795	1,012	-	-	-	7,783	-
<b>Total Assets</b>	<b>163,836</b>	<b>121,281</b>	<b>14,594</b>	<b>18,441</b>	<b>-</b>	<b>9,520</b>	<b>-</b>
<b>Liabilities</b>							
Fixed Rate Items	22,283	21,273	1,010	-	-	-	-
Variable Rate Items	-	-	-	-	-	-	-
Non rate Sensitive	-	-	-	-	-	-	-
<b>Total Liabilities</b>	<b>22,283</b>	<b>21,273</b>	<b>1,010</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Net Gap</b>		<b>100,008</b>	<b>13,584</b>	<b>18,441</b>	<b>-</b>	<b>9,520</b>	<b>-</b>
<b>Cumulative Gap</b>		<b>100,008</b>	<b>113,592</b>	<b>132,033</b>	<b>132,033</b>	<b>141,553</b>	<b>141,553</b>

## NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

### 34 RISK MANAGEMENT continued

2009	Rate profile band						
Profit Rate profile (£000)		0-1	2-3	4-6	7-12	1-5	Over 5
Bank	Total	month	months	months	months	years	years
<b>Assets</b>							
Fixed Rate Items	103,450	101,713	-	-	-	1,737	-
Variable Rate Items	51,591	18,556	14,594	18,441	-	-	-
Non rate Sensitive	7,882	906	-	-	-	6,976	-
<b>Total Assets</b>	<b>162,923</b>	<b>121,175</b>	<b>14,594</b>	<b>18,441</b>	-	<b>8,713</b>	-
<b>Liabilities</b>							
Fixed Rate Items	22,283	21,273	1,010	-	-	-	-
Variable Rate Items	-	-	-	-	-	-	-
Non rate Sensitive	-	-	-	-	-	-	-
<b>Total Liabilities</b>	<b>22,283</b>	<b>21,273</b>	<b>1,010</b>	-	-	-	-
<b>Net Gap</b>		<b>99,902</b>	<b>13,584</b>	<b>18,441</b>	-	<b>8,713</b>	-
<b>Cumulative Gap</b>		<b>99,902</b>	<b>113,486</b>	<b>131,927</b>	<b>131,927</b>	<b>140,640</b>	<b>140,640</b>

2008	Rate profile band						
Profit Rate profile (£000)		0-1	2-3	4-6	7-12	1-5	Over 5
Group	Total	month	months	months	months	years	years
<b>Assets</b>							
Fixed Rate Items	134,623	103,729	26,796	-	4,098	-	-
Variable Rate Items	94,692	32,534	22,596	39,562	-	-	-
Non rate Sensitive	44,557	973	-	-	-	4,885	38,699
<b>Total Assets</b>	<b>273,872</b>	<b>137,236</b>	<b>49,392</b>	<b>39,562</b>	<b>4,098</b>	<b>4,885</b>	<b>38,699</b>
<b>Liabilities</b>							
Fixed Rate Items	109,814	68,488	621	1,555	100	39,050	-
Variable Rate Items	-	-	-	-	-	-	-
Non rate Sensitive	-	-	-	-	-	-	-
<b>Total Liabilities</b>	<b>109,814</b>	<b>68,488</b>	<b>621</b>	<b>1,555</b>	<b>100</b>	<b>39,050</b>	-
<b>Net Gap</b>		<b>68,748</b>	<b>48,771</b>	<b>38,007</b>	<b>3,998</b>	<b>(34,165)</b>	<b>38,699</b>
<b>Cumulative Gap</b>		<b>68,748</b>	<b>117,519</b>	<b>155,526</b>	<b>159,524</b>	<b>125,359</b>	<b>164,058</b>

## NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

### 34 RISK MANAGEMENT continued

2008 Profit Rate profile (£000) Bank	Total	Rate profile band					
		0-1 month	2-3 months	4-6 months	7-12 months	1-5 years	Over 5 years
<b>Assets</b>							
Fixed Rate Items	134,623	103,729	26,796	-	4,098	-	-
Variable Rate Items	94,692	32,534	22,596	39,562	-	-	-
Non rate Sensitive	5,538	653	-	-	-	4,885	-
<b>Total Assets</b>	<b>234,853</b>	<b>136,916</b>	<b>49,392</b>	<b>39,562</b>	<b>4,098</b>	<b>4,885</b>	<b>-</b>
<b>Liabilities</b>							
Fixed Rate Items	70,764	68,488	621	1,555	100	-	-
Variable Rate Items	-	-	-	-	-	-	-
Non rate Sensitive	-	-	-	-	-	-	-
<b>Total Liabilities</b>	<b>70,764</b>	<b>68,488</b>	<b>621</b>	<b>1,555</b>	<b>100</b>	<b>-</b>	<b>-</b>
<b>Net Gap</b>		<b>68,428</b>	<b>48,771</b>	<b>38,007</b>	<b>3,998</b>	<b>4,885</b>	<b>-</b>
<b>Cumulative Gap</b>		<b>68,428</b>	<b>117,199</b>	<b>155,206</b>	<b>159,204</b>	<b>164,089</b>	<b>164,089</b>

Profit rate risk is managed within profit rate gap limits on a daily basis. The sensitivity of the Income Statement to various profit rate scenarios are considered on a daily basis. An analysis of the Group's sensitivity to an increase or decrease in market profit rates, assuming no asymmetrical movement in yield curves and a constant financial position, is as follows at the financial year end;

#### 2009

##### Group and Bank

Change in rates (Basis points)	-100 bp	-50 bp	-25 bp	+25 bp	+50 bp	+100bp
Effect on income statement £ 000	-1,336	-668	-334	+334	+668	+1,336
% of net margin*	-40	-20	-10	+10	+20	+40

#### 2008

##### Group and Bank

Change in rates (Basis points)	-100 bp	-50 bp	-25 bp	+25 bp	+50 bp	+100bp
Effect on income statement £ 000	-1,644	-822	-411	+411	+822	+1,644
% of net margin*	-21	-11	-5	+5	+11	+21

\* % of net margin represents the impact to the income statement

#### 2 Sensitivity to fair value of instruments

While the Bank does not hold or trade in profit rate products, the fair value of financial instruments held by the Bank will be affected by current market forces including profit rates. The table below sets out the sensitivity to fair values of related instruments assuming all other factors remain constant.

**34 RISK MANAGEMENT** continued

**2009**

**Group and Bank**

Change in rates (Basis points)	-100 bp	-50 bp	-25 bp	+25 bp	+50 bp	+100bp
Effect on fair value (equity) £ 000	+63	+32	+16	-16	-31	-62

There is no impact for 2008 as there were no fixed profit rate products.

**3 Currency Risk**

Currency risk is the risk of loss arising from changes in foreign exchange rates. The Board has set limits on open currency positions and these positions are monitored daily to ensure positions are maintained within the established limits.

The Bank does not take significant currency positions as all positions other than the functional currency are covered. Small residual currency exposures remain well within the Board approved limits.

**Market risk – trading**

The Bank had no trading portfolio during the years ended 31 December 2009 or 31 December 2008.

**34.5 Operational risk\***

Operational risk is the risk of loss arising from inadequate or failed systems, human error and fraud, processes and external events. Operational risks can result in damage to reputation, have legal or regulatory implications or lead to financial loss. The Bank has implemented a robust control framework to significantly mitigate these risks.

Controls include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit. Risk matrices have been developed for each department which form part of a quality self-assessment process.

\*unaudited

**34.6 Capital management and risk**

The Group's lead regulator, the Financial Services Authority ("FSA") sets and monitors capital requirements for the Group. The Group complies with the provisions of the Basel II framework in respect of regulatory capital. To calculate capital requirements the Group uses "Standardised approach" for credit risk, "Basic indicator approach" for operational risk and the "Standardised approach" for market risk.

The Group's capital represents "Tier 1" capital and includes ordinary share capital, share premium, capital redemption reserve, retained earnings, fair value reserve and foreign exchange reserve subject to other regulatory adjustments. All banking operations are categorised as "Banking book" business and accordingly the risk-weighted assets are calculated to reflect the varying levels of risks attached to assets.

The Group's primary objective and policy is to maintain a strong capital base so as to maintain investor, depositor and market confidence. The Group has complied with all regulatory (FSA) capital requirements throughout the year.

The minimum required regulatory capital under Basel II as at 31 December 2009 was £13.6m compared to the available capital base of £132.9m. The current level of capital is considered to be adequate to support future growth.

Capital and risk-reward management are the responsibility of ALCO, which monitors capital and risk limits for the various areas of the Bank's business. Currently capital is not a constraint on growth.

The FSA's approach to Basel II capital maintenance requirements is primarily based on monitoring the relationship of Capital Resources Requirement (measured as 8% of risk-weighted assets) to available capital resources. The FSA also sets Individual Capital Guidelines (ICG) for each bank/banking group that sets capital requirements in excess of the minimum Capital Resource Requirement. A key input to the ICG setting process is the Group's Internal Capital Adequacy Assessment Process (ICAAP). The Group submitted its ICAAP documents to the FSA on 8 September 2009. The agreed ICG remains confidential between each bank and the FSA in accordance with accepted practice.

## NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2009

### 35 POST BALANCE SHEET EVENTS

The Directors confirm there are no significant events arising since the balance sheet date that should be reported to shareholders.

### 36 RECONCILIATION OF AMOUNTS REFERRED TO IN CHAIRMAN'S STATEMENT

	2009	2008
	£	£
Operating (loss)/profit on continued operations before tax, fair value losses and impairments		
Operating (loss)/profit before tax on continued operations	(23,698,714)	563,861
Adjusted for:		
Fair value adjustment on assets designated as fair value through income statement	4,134,525	-
Provision for impairment of financing arrangements	6,351,575	3,750,000
Provision for impairment of available for sale securities	7,030,988	-
Impairment of goodwill	954,077	-
Oil & Gas activity:	1,180,645	-
- Gross loss	355,930	-
- Overheads	824,715	-
Operating (loss)/profit on continued operations before tax, fair value losses and impairments	<b>(4,046,904)</b>	4,313,861
Core operating expenses		
Total operating expenses	(27,068,731)	(11,540,105)
Adjusted for:		
Fair value loss on assets designated as fair value through income statement	4,134,525	-
Provision for impairment of financing arrangements	6,351,575	3,750,000
Provision for impairment of available for sale securities	7,030,988	-
Impairment of goodwill	954,077	-
Oil & Gas activity - overheads	824,715	-
Core operating expenses	<b>(7,772,851)</b>	(7,790,105)



## BANK INFORMATION

**Registered No. 5328847**

### **Directors**

Adnan Ahmed Yousif *Chairman*

Shabir Randeree *Deputy Chairman*

Salman Abbasi

Yusef Abu Khadra

Zaher Al-Ajjawi

Mohammed Al Sarhan *Senior Independent Director*

Aabed Alzeera

Subhi Benkhadra

George Morton

Keith McLeod *Acting Chief Executive Officer and Finance Director*

### **Secretary**

M A Mohaimin Chowdhury

### **Registered Office**

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London E14 5AG

### **Correspondent Bankers**

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Bahrain Islamic Bank

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Manama, Kingdom of Bahrain

### **Registrars**

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The Registry

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Kent BR3 4TU

### **Nominated Advisor and Broker**

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London EC2V 7AN

### **Solicitors**

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