

**Technikabank OJSC**

**International Financial Reporting Standards  
Consolidated Financial Statements and  
Independent Auditor's Report**

**31 December 2010**

## CONTENTS

### Independent Auditor's Report

### Financial Statements

Consolidated Statement of Financial Position .....	1
Consolidated Statement of Comprehensive Income.....	2
Consolidated Statement of Changes in Equity .....	3
Consolidated Statement of Cash Flows .....	4

### Notes to the Consolidated Financial Statements

1	Introduction.....	5
2	Operating Environment of the Group.....	6
3	Summary of Significant Accounting Policies.....	6
4	Critical Accounting Estimates and Judgements in Applying Accounting Policies .....	16
5	Adoption of New or Revised Standards and Interpretations .....	17
6	New accounting Pronouncements.....	19
7	Cash and Cash Equivalents .....	22
8	Due from Other Banks and Financial Institutions .....	23
9	Loans and Advances to Customers.....	26
10	Investment Securities Available for Sale .....	31
11	Other Investment Securities .....	32
12	Investment Properties.....	32
13	Premises, Equipment and Intangible Assets .....	33
14	Other Financial Assets .....	34
15	Other Assets.....	35
16	Due to Other Banks and Financial Institutions.....	36
17	Customer Accounts .....	36
18	Debt Securities in Issue.....	37
19	Term Borrowings from Other Banks and Financial Institutions.....	38
20	Other Financial Liabilities .....	39
21	Other Liabilities.....	39
22	Share Capital.....	40
23	Other Reserves .....	40
24	Interest Income and Expense.....	41
25	Fee and Commission Income and Expense .....	41
26	Administrative and Other Operating Expenses.....	42
27	Income Taxes.....	42
28	Earnings per Share.....	44
29	Segment Analysis.....	44
30	Financial Risk Management .....	46
31	Management of Insurance Risk.....	57
32	Management of Capital .....	58
33	Contingencies and Commitments.....	59
34	Fair Value of Financial Instruments .....	61
35	Reconciliation of Classes of Financial Instruments with Measurement Categories .....	63
36	Related Party Transactions .....	64
37	Events After the End of the Reporting Period.....	65



## ***Independent Auditor's Report***

To the Shareholders and Board of Directors of Teknikabank Open Joint Stock Company:

- 1 We have audited the accompanying consolidated financial statements of Teknikabank Commercial Bank and its subsidiaries (the "Group") which comprise the consolidated statement of financial position as of 31 December 2010 and the consolidated statements of income, comprehensive income, changes in equity and cash flows for the year then ended and a summary of significant accounting policies and other explanatory notes.

### **Management's Responsibility for the Consolidated Financial Statements**

- 2 Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditor's Responsibility**

- 3 Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.
- 4 An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
- 5 We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### **Opinion**

- 6 In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2010, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

*PricewaterhouseCoopers Audit Azerbaijan LLC*

31 May 2011  
Baku, Republic of Azerbaijan

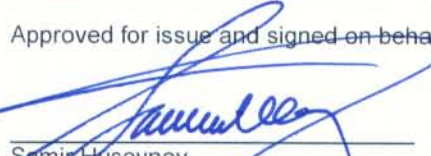
---

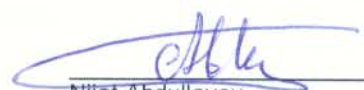
PricewaterhouseCoopers Audit Azerbaijan LLC  
The Landmark Office Plaza III, 12<sup>th</sup> floor, 90A Nizami Street  
AZ 1010, Baku, Azerbaijan  
T: +994 (12) 497 25 15, F: +994 (12) 497 74 11, [www.pwc.com/az](http://www.pwc.com/az)

**Technikabank OJSC**  
**Consolidated Statement of Financial Position**

<i>In thousands of Azerbaijani Manats</i>	<b>Note</b>	<b>2010</b>	<b>2009</b>	<b>2008</b>
<b>Assets</b>				
Cash and cash equivalents	7	45,242	47,897	49,392
Mandatory cash balances with CBAR		1,102	837	9,933
Due from other banks and financial institutions	8	5,947	6,980	15,504
Loans and advances to customers	9	353,447	342,509	318,704
Investment securities available for sale	10	853	609	550
Other investment securities	11	12,979	2,336	-
Investment properties	12	16,278	1,181	253
Premises and equipment	13	38,702	39,111	36,747
Intangible assets	13	2,243	2,628	1,251
Deferred income tax asset		-	-	-
Other financial assets	14	4,155	3,260	1,849
Other assets	15	8,780	2,858	3,494
<b>Total assets</b>		<b>489,728</b>	<b>450,206</b>	<b>437,677</b>
<b>Liabilities</b>				
Due to other banks and financial institutions	16	19,669	28,826	75,570
Customer accounts	17	271,386	189,812	174,603
Debt securities in issue	18	3,337	10,906	31,271
Term borrowings from other banks and financial institutions	19	125,198	157,007	99,739
Current income tax liability		497	-	861
Deferred income tax liability	27	-	971	1,363
Provision on credit related instruments	33	291	176	-
Other financial liabilities	20	602	1,740	4,007
Other liabilities	21	1,823	2,173	1,404
<b>Total liabilities</b>		<b>422,803</b>	<b>391,611</b>	<b>388,818</b>
<b>Equity</b>				
Share capital	22	53,685	41,712	26,912
Share premium	22	3,464	3,464	3,464
Revaluation reserve for premises	23	3,049	3,143	15,804
Revaluation reserve for investment available for sale	23	118	149	2,589
Retained earnings		6,609	10,127	90
<b>Total equity</b>		<b>66,925</b>	<b>58,595</b>	<b>48,859</b>
<b>Total liabilities and equity</b>		<b>489,728</b>	<b>450,206</b>	<b>437,677</b>

Approved for issue and signed on behalf of the Board of Directors on 31 May 2011:

  
 Samir Huseynov  
 Chairman of the Board of Directors

  
 Nijat Abdullayev  
 Head of Finance Department



**Technikabank OJSC**  
**Consolidated Statement of Comprehensive Income**

<i>In thousands of Azerbaijani Manats</i>	<b>Note</b>	<b>2010</b>	<b>2009</b>
Interest income	24	49,662	53,716
Interest expense	24	(26,576)	(27,527)
<b>Net interest income</b>		<b>23,086</b>	<b>26,189</b>
Provision for loan impairment	9	(12,690)	(9,584)
Reversal of provision of/(provision charge for) due from other banks	8	1,190	(1,778)
<b>Net interest income after provision for loan impairment</b>		<b>11,586</b>	<b>14,827</b>
Fee and commission income	25	10,390	10,504
Fee and commission expense	25	(2,522)	(2,355)
Gains less losses from trading in foreign currencies		1,867	854
Gain on revaluation of investment properties		-	111
Loss on revaluation of premises		-	(2,388)
Foreign exchange translation gains less losses		1,618	648
Insurance premiums written		2,228	926
Reinsurance premiums ceded		(314)	(87)
Decrease/(Increase) of provision for unearned premiums		52	278
Increase of reinsurer's share of provision for unearned premiums		(282)	(89)
Claims incurred		(294)	(262)
Provision for losses on credit related commitments		(115)	(176)
Other operating income		60	41
Impairment of repossessed assets		(477)	-
Administrative and other operating expenses	26	(15,909)	(14,333)
<b>Profit before tax</b>		<b>7,888</b>	<b>8,499</b>
Income tax credit	27	473	544
<b>Profit for the year</b>		<b>8,361</b>	<b>9,043</b>
<b>Other comprehensive income:</b>			
Available-for-sale investments:			
- Losses less gains/(gains less losses)	23	(31)	59
Revaluation of premises and equipment	23	-	793
Income tax recorded directly in other comprehensive income	23	-	(159)
<b>Other comprehensive (loss)/income for the year</b>		<b>(31)</b>	<b>693</b>
<b>Total comprehensive income for the year</b>		<b>8,330</b>	<b>9,736</b>
<b>Earnings per share for profit attributable to the equity holders of the Group, basic and diluted</b>	28	<b>0.156</b>	<b>0.168</b>



**Technikabank OJSC**  
**Consolidated Statement of Changes in Equity**

<i>In thousands of Azerbaijani Manats</i>	Note	Share capital	Share premium	Other Reserves	Retained earnings	Total equity
Balance at 1 January 2009		26,912	3,464	2,679	15,804	48,859
Total comprehensive income for 2009		-	-	693	9,043	9,736
Transfer to retained earnings		-	-	(80)	80	-
Balance at 31 December 2009		41,712	3,464	3,292	10,127	58,595
Total comprehensive income for 2010		-	-	(31)	8,361	8,330
Transfer to retained earnings		-	-	(94)	94	-
Share issue		11,973	-	-	(11,973)	-
Balance at 31 December 2010		53,685	3,464	3,167	6,609	66,925

**Technikabank OJSC**  
**Consolidated Statement of Cash Flows**

<i>In thousands of Azerbaijani Manats</i>	<i>Note</i>	<b>2010</b>	<b>2009</b>
<b>Cash flows from operating activities</b>			
Interest received		37,649	40,941
Interest paid		(24,970)	(28,142)
Fees and commissions received		10,564	9,835
Fees and commissions paid	25	(2,522)	(2,355)
Insurance premium received		1,976	846
Reinsurance premium ceded		(314)	(87)
Insurance claims paid		(294)	(262)
Income received from trading in foreign currencies		1,867	854
Other operating income received		60	41
Staff costs paid		(6,942)	(6,361)
Administrative and other operating expenses		(4,862)	(4,105)
Income tax paid		-	(861)
<b>Cash flows from operating activities before changes in operating assets and liabilities</b>		<b>12,212</b>	<b>10,344</b>
<b>Changes in operating assets and liabilities</b>			
Net (increase)/decrease in mandatory cash balances with the CBAR		(265)	9,096
Net decrease in due from other banks		2,609	7,266
Net increase in loans and advances to customers		(13,211)	(22,078)
Net increase in other investment securities	11	(10,643)	(2,336)
Net increase in other financial assets		(1,069)	(742)
Net (increase)/decrease in other assets		(687)	716
Net decrease in due to other banks and financial institutions		(9,202)	(46,625)
Net increase in customer accounts		79,984	14,970
Net decrease in other financial liabilities		(1,138)	(2,363)
Net (decrease)/ increase in other liabilities		(299)	519
<b>Net cash provided from/(used in) operating activities</b>		<b>58,291</b>	<b>(31,233)</b>
<b>Cash flows from investing activities</b>			
Acquisition of premises and equipment and intangible assets		(7,299)	(9,491)
Acquisition of investment securities available for sale		(274)	-
Acquisition of investment properties	12	(15,650)	-
<b>Net cash used in investing activities</b>		<b>(23,223)</b>	<b>(9,491)</b>
<b>Cash flows from financing activities</b>			
Proceeds from term borrowings from other banks and financial institutions		83,943	122,071
Repayment of term borrowings from other banks and financial institutions		(115,698)	(64,288)
Repayment of debt securities in issue		(7,630)	(19,137)
<b>Net cash (used in)/provided from financing activities</b>		<b>(39,385)</b>	<b>38,646</b>
<b>Effect of exchange rate changes on cash and cash equivalents</b>		<b>1,662</b>	<b>583</b>
<b>Net decrease in cash and cash equivalents</b>		<b>(2,655)</b>	<b>(1,495)</b>
Cash and cash equivalents at the beginning of the year		47,897	49,392
<b>Cash and cash equivalents at the end of the year</b>	<b>7</b>	<b>45,242</b>	<b>47,897</b>

## 1 Introduction

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards for the year ended 31 December 2010 for Technikabank OJSC (the "Bank") and its subsidiaries (together referred to as the "Group").

The Bank was incorporated on 14 December 1993 and is domiciled in the Republic of Azerbaijan. The Bank is an open joint stock company limited by shares and was set up in accordance with Azerbaijani regulations.

**Principal activity.** The Bank's principal business activity is commercial and retail banking operations within the Republic of Azerbaijan. The Bank has operated under a full banking licence issued by the Central Bank of the Republic of Azerbaijan ("CBAR") since 1994. The Bank participates in the state deposit insurance scheme, which was introduced by the Azerbaijani Law, "Deposits of individuals insurance in the Republic of Azerbaijan" dated 29 December 2006. The State Deposit Insurance Fund guarantees repayment of all individual deposits up to the amounts described below:

- until 1 January 2008 – up to AZN 4,000;
- from 1 January 2008 until 1 January 2010 – up to AZN 6,000;
- 1 January 2010 and afterwards – up to AZN 30,000.

The amounts over respective limits are not insured.

The legal owner and ultimate controlling party of the Group is the majority shareholder, World Wines, a private company registered in the Republic of Azerbaijan, and its controlling party, Mr. Adil Mammadov. However, it has been entrusted to Mr. Etibar Aliyev to continue running the business with control over all day-to-day activities together with longer term strategic planning of the Group. World Wines' registered address is Azizbeyov district, Yesenin str. 11, apt. 4, Baku, Republic of Azerbaijan.

The Group includes four subsidiaries fully owned by the Bank and operating in the brokerage, leasing, insurance and card processing industries respectively.

On 16 May 2002, the Group registered its fully-owned subsidiary, Capital Management Limited LLC ("Capital Management") at the Ministry of Justice of the Republic of Azerbaijan. On 14 March 2003, Capital Management was granted a brokerage licence by the State Committee on Securities to render brokerage services at Baku Stock Exchange.

On 2 June 2004, the Group registered its fully-owned subsidiary, TechnikaLeasing LLC ("TechnikaLeasing") at the Ministry of Justice of the Republic of Azerbaijan. TechnikaLeasing commenced its operations in late 2005.

On 12 December 2006, the Group acquired 100% of the share capital of Alfa Insurance OJSC ("Alfa Insurance"). Alfa Insurance was formed on 28 August 1997 rendering insurance products including auto, health and property insurance.

On 28 December 2009, the Group acquired 100% of the share capital of Texkart OJSC ("Texkart"). Texkart was formed on 2 August 2007 and acts as a clearing and authorisation centre for plastic card transactions in the Republic of Azerbaijan.

The Bank has 35 (31 December 2009: 35) branches and 2 (31 December 2009: 2) service points within the Republic of Azerbaijan.

The Group had 626 employees as at 31 December 2010 (31 December 2009: 673).

**Registered address and place of business.** The Bank's registered address is:

Narimanov district, Ataturk Avenue, 1107  
AZ1069  
Baku  
Republic of Azerbaijan

**Presentation currency.** These consolidated financial statements are presented in thousands of Azerbaijani Manats ("AZN thousands").



## 2 Operating Environment of the Group

The Republic of Azerbaijan displays certain characteristics of an emerging market, including existence of a currency that is in practice not convertible in most countries outside of the Republic of Azerbaijan, restrictive currency controls and relatively high inflation. The banking sector in the Republic of Azerbaijan is sensitive to adverse fluctuations in confidence and economic conditions and may occasionally experience reductions in liquidity. Management is unable to predict economic trends and developments in the banking sector and consequently what effect, if any, a deterioration in the liquidity of or confidence in the Azerbaijani banking system could have on the financial position of the Group.

The tax, currency and customs legislation within the Republic of Azerbaijan is subject to varying interpretations, and changes, which can occur frequently. Furthermore, the need for further developments in the bankruptcy laws, the absence of formalised procedures for the registration and enforcement of collateral, and other legal and fiscal impediments contribute to the difficulties experienced by banks currently operating in the Republic of Azerbaijan. The future economic direction of the Republic of Azerbaijan is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory, and political developments.

**Recent volatility in global financial markets.** The ongoing global financial crisis which commenced in the middle of 2007 has resulted in, among other things, a lower level of capital market funding, at times much higher than normal interbank lending rates, and lower liquidity levels across the Republic of Azerbaijan banking sector resulting in a significant reduction in the new number of new loans and advances made to customers, and higher funding costs where it remains possible to obtain debt finance from International Institutions or other local banks. The uncertainties in the global financial market have also led to bank failures and bank rescues in the United States of America, Western Europe and in Russia. Such circumstances could affect the ability of the Group to obtain new borrowings and re-finance its existing borrowings at terms and conditions similar to those applied to earlier transactions. The borrowers of the Group may also be affected by the lower liquidity situation which could in turn impact their ability to repay their outstanding loans. Deteriorating operating conditions for borrowers may also have an impact on Management's cash flow forecasts and assessment of the impairment of financial and non-financial assets. To the extent that information is available, Management has reflected revised estimates of expected future cash flows in their impairment assessments.

Management is unable to reliably estimate the effects on the Group's financial position of any further deterioration in the liquidity of the financial markets and the increased volatility in the currency and equity markets. Management believes it is taking all the necessary measures to support the sustainability and growth of the Group's business in the current circumstances.

## 3 Summary of Significant Accounting Policies

**Basis of Preparation.** These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") under the historical cost convention, as modified by the revaluation of premises and investment properties, and the valuation at fair value of investment securities available for sale. The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the periods presented. Management, being the Board of Directors, who approved these consolidated financial statements for issue, have the power to amend these consolidated financial statements. Any such change requires the approval of the Board of Directors.

**Consolidated financial statements.** Subsidiaries are those companies and other entities (including special purpose entities) in which the Group, directly or indirectly, has an interest of more than one half of the voting rights or otherwise has power to govern the financial and operating policies so as to obtain benefits. Subsidiaries are consolidated from the date on which control is transferred to the Group (acquisition date) and are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries. The cost of an acquisition is measured at the fair value of the assets given up, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. The date of exchange is the acquisition date where a business combination is achieved in a single transaction, and is the date of each share purchase where a business combination is achieved in stages by successive share purchases.

### 3 Summary of Significant Accounting Policies (Continued)

The excess of the cost of acquisition over the acquirer's share of the fair value of the net assets of the acquiree at each exchange transaction is recorded as goodwill. The excess of the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities acquired over cost ("negative goodwill") is recognised immediately in profit or loss for the year.

Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured at their fair values at the acquisition date, irrespective of the extent of any minority interest. The difference, if any, between the fair values of the net assets at the dates of exchange and at the date of acquisition is recorded directly in equity.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated; unrealised losses are also eliminated unless the cost cannot be recovered. The Bank and all of its subsidiaries use uniform accounting policies consistent with the Group's policies.

**Key measurement terms.** Depending on their classification financial instruments are carried at fair value or amortised cost as described below.

*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. Fair value is the current bid price for financial assets and current asking price for financial liabilities, which are quoted in an active market. For assets and liabilities with offsetting market risks, the Group may use mid-market prices as a basis for establishing fair values for the offsetting risk positions and apply the bid or asking price to the net open position as appropriate.

A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange or other institution and those prices represent actual and regularly occurring market transactions on an arm's length basis.

Valuation techniques such as discounted cash flows models or models based on recent arms length transactions or consideration of financial data of the investees are used to fair value certain financial instruments, for which external market pricing information is not available. Valuation techniques may require assumptions not supported by observable market data. Disclosures are made in these consolidated financial statements if changing any such assumptions to a reasonably possible alternative would result in significantly different profit, income, total assets or total liabilities.

*Transaction costs* are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial instrument. An incremental cost is one that would not have been incurred if the transaction had not taken place. Transaction costs include fees and commissions paid to agents (including employees acting as selling agents), advisors, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Transaction costs do not include debt premiums or discounts, financing costs or internal administrative or holding costs.

*Amortised cost* is the amount, at which the financial instrument was recognised at initial recognition less any principal repayments, plus accrued interest, and for financial assets less any write-down for incurred impairment losses. Accrued interest includes amortisation of transaction costs deferred at initial recognition and of any premium or discount to maturity amount, using the effective interest method. Accrued interest income and accrued interest expense, including both accrued coupon and amortised discount or premium (including fees deferred at origination, if any), are not presented separately and are included in the carrying values of related consolidated statement of financial position items.

### 3 Summary of Significant Accounting Policies (Continued)

*The effective interest method* is a method of allocating interest income or interest expense over the relevant period so as to achieve a constant periodic rate of interest (effective interest rate) on the carrying amount. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts (excluding future credit losses) through the expected life of the financial instrument or a shorter period, if appropriate, to the net carrying amount of the financial instrument. The effective interest rate discounts cash flows of variable interest instruments to the next interest re-pricing date, except for the premium or discount, which reflects the credit spread over the floating rate specified in the instrument, or other variables that are not reset to market rates. Such premiums or discounts are amortised over the whole expected life of the instrument. The present value calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate (refer to income and expense recognition policy).

**Initial recognition of financial instruments.** Trading securities, derivatives and other financial instruments at fair value through profit or loss are initially recorded at fair value. All other financial instruments are initially recorded at fair value plus transaction costs. Fair value at initial recognition is best evidenced by a transaction price. A gain or loss on initial recognition is only recorded if there is a difference between fair value and a transaction price, which can be evidenced by other observable current market transactions in the same instrument, or by a valuation technique whose inputs include only data from observable markets.

All purchases and sales of financial assets that require delivery within the time-frame established by regulation or market convention ("regular way" purchases and sales) are recorded at trade date, which is the date that the Group commits to deliver a financial asset. All other purchases are recognised when the entity becomes a party to the contractual provisions of the instrument.

**Cash and cash equivalents.** Cash and cash equivalents are items, which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Cash and cash equivalents include all inter-bank placements with original maturities of less than three months. Funds restricted for a period of more than three months are excluded from cash and cash equivalents. Cash and cash equivalents are carried at amortised cost.

**Mandatory cash balances with the CBAR.** Mandatory cash balances with the CBAR are carried at amortised cost and represent non interest bearing mandatory reserve deposits, which are not available to finance the Group's day to day operations and hence are not considered as part of cash and cash equivalents for the purposes of the consolidated cash flow statement.

**Due from other banks.** Amounts due from other banks are recorded when the Group advances money to counterparty banks with no intention of trading the resulting unquoted non-derivative receivable due on fixed or determinable dates. Amounts due from other banks are carried at amortised cost.

**Loans and advances to customers.** Loans and advances to customers are recorded when the Group advances money to purchase or originate an unquoted non-derivative receivable from a customer due on fixed or determinable dates and has no intention of trading the receivable. Loans and advances to customers are carried at amortised cost.

**Impairment of financial assets carried at amortised cost.** Impairment losses are recognised in profit or loss when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of the financial asset and which have an impact on the amount or timing of the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. If the Group determines that no objective evidence exists that impairment was incurred for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. The primary factors that the Group considers whether a financial asset is impaired is its overdue status and realisability of related collateral, if any. The following other principal criteria are also used to determine that there is objective evidence that an impairment loss has occurred:

### 3 Summary of Significant Accounting Policies (Continued)

- any instalment is overdue and the late payment cannot be attributed to a delay caused by the settlement systems;
- the borrower experiences a significant financial difficulty as evidenced by borrower's financial information that the Group obtains;
- the borrower considers bankruptcy or a financial reorganisation;
- there is adverse change in the payment status of the borrower as a result of changes in the national or local economic conditions that impact the borrower; and
- the value of collateral significantly decreases as a result of deteriorating market conditions.

For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics. Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets and the experience of management in respect of the extent, to which amounts will become overdue as a result of past loss events, and the success of recovery of overdue amounts. Past experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect past periods and to remove the effects of past conditions that do not exist currently.

Impairment losses are recognised through an allowance account to write down the asset's carrying amount to the present value of expected cash flows (which exclude future credit losses that have not been incurred) discounted at the original effective interest rate of the asset. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account through profit or loss for the year.

Uncollectible assets are written off against the related impairment loss provision after all the necessary procedures to recover the asset have been completed and the amount of the loss has been determined.

***Repossessed collateral.*** Repossessed collateral represents financial and non-financial assets acquired by the Group in settlement of overdue loans. The assets are initially recognised at fair value when acquired and included in premises and equipment, other financial assets or inventories within other assets depending on their nature and the Group's intention in respect of recovery of these assets and are subsequently remeasured and accounted for in accordance with the accounting policies for these categories of assets.

***Credit related commitments.*** The Group enters into credit related commitments, including letters of credit and financial guarantees. Financial guarantees represent irrevocable assurances to make payments in the event that a customer cannot meet its obligations to third parties and carry the same credit risk as loans. Financial guarantees and commitments to provide a loan are initially recognised at their fair value, which is normally evidenced by the amount of fees received. This amount is amortised on a straight line basis over the life of the commitment, except for commitments to originate loans if it is probable that the Group will enter into a specific lending arrangement and does not expect to sell the resulting loan shortly after origination; such loan commitment fees are deferred and included in the carrying value of the loan on initial recognition. At the end of each reporting period, the commitments are measured at the higher of (i) the unamortised balance of the amount at initial recognition and (ii) the best estimate of expenditure required to settle the commitment at end of reporting period.

### 3 Summary of Significant Accounting Policies (Continued)

**Investment securities available for sale.** This classification includes investment securities, which the Group intends to hold for an indefinite period of time and which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

Investment securities available for sale are carried at fair value. Interest income on available for sale debt securities is calculated, using the effective interest method and recognised in profit or loss for the year. Dividends on available-for-sale equity instruments are recognised in profit or loss for the year when the Group's right to receive payment is established and it is probable that the dividends will be collected. All other elements of changes in the fair value are recognised in other comprehensive income until the investment is derecognised or impaired, at which time the cumulative gain or loss is reclassified from other comprehensive income to profit or loss for the year.

Impairment losses are recognised in profit or loss for the year when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of investment securities available for sale. A significant or prolonged decline in the fair value of an equity security below its cost is an indicator that it is impaired. The cumulative impairment loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that asset previously recognised in profit or loss – is reclassified from other comprehensive income to profit or loss for the year. Impairment losses on equity instruments are not reversed and any subsequent gains are recognised in other comprehensive income. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through profit or loss for the year.

**Derecognition of financial assets.** The Group derecognises financial assets when (a) the assets are redeemed or the rights to cash flows from the assets otherwise expired or (b) the Group has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement while (i) also transferring substantially all the risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all risks and rewards of ownership but not retaining control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale.

**Investment properties.** Investment property is property held by the Group to earn rental income or for capital appreciation and which is not occupied by the Group.

Investment property is initially recognised at cost, including transaction costs, and subsequently re-measured at fair value based on its market value. The fair value of the Group's investment property is obtained from reports of independent appraisers, who hold a recognised and relevant professional qualification and who have recent experience in valuation of property of similar location and category. Investment property that is being redeveloped for continuing use as investment property or for which the market has become less active continues to be measured at fair value. Earned rental income is recorded in profit or loss within other operating income. Gains and losses resulting from changes in the fair value of investment property are recorded in profit or loss and presented separately.

Subsequent expenditure is capitalised only when it is probable that future economic benefits associated with it will flow to the Group and the cost can be measured reliably. All other repairs and maintenance costs are expensed when incurred. If an investment property becomes owner-occupied, it is reclassified to premises and equipment, and its carrying amount at the date of reclassification becomes its deemed cost to be subsequently depreciated.

**Premises and equipment.** Premises and equipment are stated at cost, or revalued amounts, as described below, less accumulated depreciation and provision for impairment, where required. Cost of premises and equipment of acquired subsidiaries is the estimated fair value at the date of acquisition.

### 3 Summary of Significant Accounting Policies (Continued)

Premises of the Group are subject to revaluation on a regular basis. The frequency of revaluation depends upon the movements in the fair values of the premises being revalued. The revaluation reserve for premises included in equity is transferred directly to retained earnings when the surplus is realised, i.e. either on the retirement or disposal of the asset, or as the asset is used by the Group; in the latter case, the amount of the surplus realised is the difference between depreciation based on the revalued carrying amount of the asset and depreciation based on the asset's original cost.

Construction in progress is carried at cost, less provision for impairment where required. Cost includes borrowing costs incurred on specific or general funds borrowed to finance construction of qualifying assets. Upon completion, assets are transferred to premises and equipment at their carrying amount. Construction in progress is not depreciated until the asset is available for use.

All other items of premises and equipment are stated at cost less accumulated depreciation and impairment losses, if any.

Costs of minor repairs and maintenance are expensed when incurred. Cost of replacing major parts or components of premises and equipment items are capitalised and the replaced part is retired.

If impaired, premises and equipment are written down to the higher of their value in use and fair value less costs to sell. The decrease in carrying amount is charged to profit or loss to the extent it exceeds the previous revaluation surplus in equity.

An impairment loss recognised for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's value in use or fair value less costs to sell.

Gains and losses on disposals determined by comparing proceeds with carrying amount are recognised in profit or loss.

**Depreciation.** Land is not depreciated. Depreciation on other items of premises and equipment is calculated using the straight-line method to allocate their cost or revalued amounts to their residual values over their estimated useful lives at the following annual rates:

Premises	3%;
Computers and communication equipment	25%;
Furniture, fixtures and other equipment	20%;
Motor vehicles	25%; and
Leasehold improvements	over the term of the underlying lease.

The residual value of an asset is the estimated amount that the Group would currently obtain from disposal of the asset less the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life. The residual value of an asset is nil if the Group expects to use the asset until the end of its physical life. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

**Intangible assets.** All of the Group's intangible assets have definite useful life and include capitalised computer software.

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. Development costs that are directly associated with identifiable and unique software controlled by the Group are recorded as intangible assets if inflow of incremental economic benefits exceeding costs is probable. All other costs associated with computer software, e.g. its maintenance, are expensed when incurred. Capitalised computer software is amortised on a straight line basis over expected useful lives of 4 to 5 years.

**Operating leases.** Where the Group is a lessee in a lease, which does not transfer substantially all the risks and rewards incidental to ownership from the lessor to the Group, the total lease payments are charged to profit or loss on a straight-line basis over the period of the lease.



### 3 Summary of Significant Accounting Policies (Continued)

**Finance leases.** Where the Group is a lessor in a lease, which transfers substantially all the risks and rewards incidental to ownership to the lessee, the assets leased out are presented as a finance lease receivable and carried at the present value of the future lease payments. Finance lease receivables are initially recognised at commencement (when the lease term begins), using a discount rate determined at inception (the earlier of the date of the lease agreement and the date of commitment by the parties to the principal provisions of the lease).

The difference between the gross receivable and the present value represents unearned finance income. This income is recognised over the term of the lease using the net investment method (before tax), which reflects a constant periodic rate of return. Incremental costs directly attributable to negotiating and arranging the lease are included in the initial measurement of the finance lease receivable and reduce the amount of income recognised over the lease term. Finance income from leases is recorded within interest income in the consolidated statement of comprehensive income.

Impairment losses are recognised in profit or loss when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of finance lease receivables. The Group uses the same principal criteria to determine that there is objective evidence that an impairment loss has occurred as for loans carried at amortised costs disclosed earlier in this note. Impairment losses are recognised through an allowance account to write down the receivables' net carrying amount to the present value of expected cash flows (which exclude future credit losses that have not been incurred) discounted at the interest rates implicit in the finance leases. The estimated future cash flows reflect the cash flows that may result from obtaining and selling the assets subject to the lease.

#### **Non-life insurance operations**

- **Premiums written.** Upon inception of a contract, insurance premium is recorded as written and a corresponding provision for unearned premium is created.
- **Provision for unearned premiums.** Provision for unearned premiums represents the proportion of premiums written in the year that relate to unexpired terms of policies in force as at the balance sheet date. Re-insurers' share of provision for unearned premiums represents the proportion of premiums ceded in the year that relate to unexpired terms of policies in force as at the balance sheet date. The provision for unearned premiums, net of re-insurers' share of provision, is released to income on a time proportion basis, using straight line method.
- **Claims paid.** Claims paid including claims handling expenses are charged to the consolidated statement of income as incurred.
- **Loss provision.** Loss provision represents the accumulation of estimates for incurred losses and includes outstanding claims provision ("OCP") and provision for losses incurred, but not yet reported ("IBNR"). Estimates of claims handling expenses are included in both OCP and IBNR. OCP is provided in respect of claims reported, but not settled as at the balance sheet date. The estimation is made on the basis of information received by the Group during investigation of insurance cases expected to be settled after the balance sheet date. IBNR is actuarially determined by the Group by line of business, using simplified Bornhuetter-Ferguson method, based on implied expected ultimate loss ratios and implied reported claims development factors, and includes assumptions based on prior years' claims and claims handling experience. The methods of determining such estimates and establishing the resulting provisions are continually reviewed and updated. Resulting adjustments are reflected in the consolidated statement of income as they arise. The loss reserves are estimated on an undiscounted basis due to the relatively quick pattern of claims notification and payment.

### 3 Summary of Significant Accounting Policies (Continued)

- **Reinsurance.** The Group assumes and cedes reinsurance in the normal course of business. Ceded reinsurance contracts do not relieve the Group from its obligations to policyholders. Reinsurance receivables include balances due from reinsurance companies for paid claims, including claims handling expenses, and premiums ceded to the Group. Amounts recoverable from re-insurers are estimated in a manner consistent with the claim liability associated with the reinsured policy. Reinsurance payables are obligations of the Group for the transfer of reinsurance premiums to re-insurers and of the Group's share in claims in respect of insurance cases reinsured by the Group. Reinsurance contracts that do not transfer insurance risk are accounted for directly through the consolidated balance sheet and are included in other receivables or payables.
- **Deferred acquisition costs.** Acquisition costs, representing commissions and certain other underwriting expenses, which vary with and are incurred in connection with the acquisition or renewal of insurance policies, are deferred and amortised over the period, in which the related written premiums are earned. Deferred acquisition costs are calculated separately for each line of business and are reviewed by line of business at the time of the policy issue and at the end of each accounting period to ensure they are recoverable based on future estimates.
- **Insurance related payables.** All payables are accounted for on an accruals basis. Reinsurance receivables and payables are offset where the legal right for this offset exists. Claims in the process of settlement include the amounts payable by the Group to its customers under claims that have been processed, evaluated and approved for repayment under the Group's policy.

**Due to other banks.** Amounts due to other banks are recorded when money or other assets are advanced to the Group by counterparty banks. The non-derivative liability is carried at amortised cost. If the Group purchases its own debt, it is removed from the consolidated statement of financial position and the difference between the carrying amount of the liability and the consideration paid is included in gains or losses arising from retirement of debt.

**Customer accounts.** Customer accounts are non-derivative liabilities to individuals, state or corporate customers and are carried at amortised cost.

**Debt securities in issue.** Debt securities in issue include promissory notes, bonds, certificates of deposit and debentures issued by the Group. Debt securities are stated at amortised cost. If the Group purchases its own debt securities in issue, they are removed from the statement of financial position and the difference between the carrying amount of the liability and the consideration paid is included in gains arising from retirement of debt.

**Term borrowings from other banks and financial institutions.** Term borrowings from other banks and financial institutions are carried at amortised cost.

**Derivative financial instruments.** Derivative financial instruments, including foreign exchange contracts, interest rate futures, forward rate agreements, currency and interest rate swaps, currency and interest rate options are carried at their fair value.

All derivative instruments are carried as assets when fair value is positive and as liabilities when fair value is negative. Changes in the fair value of derivative instruments are included in profit or loss for the year (gains less losses on derivatives). The Group does not apply hedge accounting.

Certain derivative instruments embedded in other financial instruments are treated as separate derivative instruments when their risks and characteristics are not closely related to those of the host contract.

**Income taxes.** Income taxes have been provided for in the consolidated financial statements in accordance with Azerbaijani legislation enacted or substantively enacted by the balance sheet date. The income tax charge comprises current tax and deferred tax and is recognised in the consolidated income statement, except if it is recognised directly in equity because it relates to transactions that are also recognised, in the same or a different period, directly in equity.

Current tax is the amount expected to be paid to or recovered from the taxation authorities in respect of taxable profits or losses for the current and prior periods. Taxable profits or losses are based on estimates if consolidated financial statements are authorised prior to filing relevant tax returns. Taxes, other than on income, are recorded within administrative and other operating expenses.

### 3 Summary of Significant Accounting Policies (Continued)

Deferred income tax is provided using the balance sheet liability method for temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit. Deferred tax balances are measured at tax rates enacted or substantively enacted at the balance sheet date, which are expected to apply to the period when the temporary differences will reverse or the tax loss carry forwards will be utilised. Deferred tax assets and liabilities are netted only within the individual companies of the Group. Deferred tax assets for deductible temporary differences are recorded only to the extent that it is probable that future taxable profit will be available, against which the deductions can be utilised.

Deferred income tax is provided on post acquisition retained earnings of subsidiaries, except where the Group controls the subsidiary's dividend policy and it is probable that the difference will not reverse through dividends or otherwise in the foreseeable future.

**Provisions for liabilities and charges.** Provisions for liabilities and charges are non-financial liabilities of uncertain timing or amount. They are accrued when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

**Trade and other payables.** Trade payables are accrued when the counterparty performed its obligations under the contract and are carried at amortised cost.

**Share premium.** When shares are issued, the excess of contributions received, net of transaction costs, over the nominal value of the shares issued is recorded as share premium in equity.

**Dividends.** Dividends are recorded in equity in the period, in which they are declared. Dividends declared after the end of the reporting period and before the consolidated financial statements are authorised for issue are disclosed in the subsequent events note. The statutory accounting reports of the Group are the basis for profit distribution and other appropriations. Azerbaijani legislation identifies the basis of distribution as the current year net profit.

**Income and expense recognition.** Interest income and expense are recorded in the consolidated statement of comprehensive income for all debt instruments on an accrual basis, using the effective interest method. This method defers, as part of interest income or expense, all fees paid or received between the parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Fees integral to the effective interest rate include origination fees received or paid by the entity relating to the creation or acquisition of a financial asset or issuance of a financial liability, for example fees for evaluating creditworthiness, evaluating and recording guarantees or collateral, negotiating the terms of the instrument and for processing transaction documents. Commitment fees received by the Group to originate loans at market interest rates are integral to the effective interest rate if it is probable that the Group will enter into a specific lending arrangement and does not expect to sell the resulting loan shortly after origination. The Group does not designate loan commitments as financial liabilities at fair value through profit or loss.

When loans and other debt instruments become doubtful of collection, they are written down to present value of expected cash inflows and interest income is thereafter recorded for the unwinding of the present value discount based on the asset's effective interest rate, which was used to measure the impairment loss.

All other fees, commissions and other income and expense items are generally recorded on an accrual basis by reference to completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided.

**Foreign currency translation.** The functional currency of each of the Group's consolidated entities is the currency of the primary economic environment, in which the entity operates. The functional currency of all

### 3 Summary of Significant Accounting Policies (Continued)

of the Group's entities and the Group's presentation currency is the national currency of the Republic of Azerbaijan, Azerbaijani Manats ("AZN").

Monetary assets and liabilities are translated into each entity's functional currency at the official exchange rate of the CBAR at the respective balance sheet dates. Foreign exchange gains and losses resulting from the settlement of the transactions and from the translation of monetary assets and liabilities into each entity's functional currency at year-end official exchange rates of the CBAR are recognised in profit or loss. Translation at year-end rates does not apply to non-monetary items, including equity investments. Effects of exchange rate changes on the fair value of equity securities are recorded as part of the fair value gain or loss.

At 31 December 2010, the principal rate of exchange used for translating foreign currency balances was USD 1 = AZN 0.7979 (2009: USD 1 = AZN 0.8031).

**Offsetting.** Financial assets and liabilities are offset and the net amount reported in the consolidated statement of financial position only when there is a legally enforceable right to offset the recognised amounts, and there is an intention to either settle on a net basis, or to realise the asset and settle the liability simultaneously.

**Staff costs and related contributions.** Wages, salaries, contributions to the Republic of Azerbaijan state pension and social insurance funds, paid annual leave and sick leave, bonuses, and non-monetary benefits are accrued in the year, in which the associated services are rendered by the employees of the Group.

**Segment reporting.** Operating segments are reported in a manner consistent with the internal reporting provided to the Group's chief operating decision maker. Segments whose revenue, result or assets are ten percent or more of all the segments are reported separately.

**Changes in presentation.** Where necessary, corresponding figures have been adjusted to conform to the presentation of the current year amounts.

The effect of reclassifications for presentation purposes was as follows on amounts at 31 December 2009:

<i>In thousands of Azerbaijani Manats</i>	As originally presented	Reclassification	As reclassified at 31 December 2009
Other financial assets	3,340	(80)	3,260
Other assets	2,778	80	2,858
Other financial liabilities	1,916	(176)	1,740
Provision on credit related instruments	-	176	176

The effect of reclassifications for presentation purposes was as follows on amounts at 1 January 2009:

<i>In thousands of Azerbaijani Manats</i>	As originally presented	Reclassification	As reclassified at 1 January 2009
Other financial assets	1,849	(290)	1,559
Other assets	4,040	290	4,330

The third consolidated statement of financial position as of 1 January 2009 is presented in these consolidated financial statements as a result of the above described changes in presentation. This requirement to present the additional opening statement of financial position, when the entity has made a restatement or reclassification, extends to the information in the related notes. Management considered materiality and concluded that it is sufficient for an entity to present such information only in those notes that have been impacted by a restatement or a reclassification and state in the consolidated financial statements that the other notes have not been impacted by the restatement or reclassification. The omission of the notes to the additional opening statement of financial position is therefore, in management's view, not material.

### 3 Summary of Significant Accounting Policies (Continued)

The reclassifications had an impact on information in notes Other financial assets, Other assets, Other financial liabilities, Provision on credit related instruments and had no impact on any other captions in the financial statements and related note disclosures.

**Amendments of the financial statements after issue.** The Bank's shareholders and management have the power to amend the financial statements after issue.

### 4 Critical Accounting Estimates and Judgements in Applying Accounting Policies

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Management also makes certain judgements, apart from those involving estimations, in the process of applying the accounting policies. Judgements that have the most significant effect on the amounts recognised in the consolidated financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include:

**Going concern.** Management have prepared these consolidated financial statements on a going concern basis. In making this judgement management have considered the current macroeconomic environment for financial institutions operating in the Republic of Azerbaijan, the profitability of operations and access to foreign financial resources as required. As disclosed in Note 30 to these consolidated financial statements, the Group has a negative net liquidity gap in the period up to twelve months as at 31 December 2010 in the amount of AZN 25,868 thousand. Therefore, management is confident that the Group will be able to obtain required funds in order to replace attracted liabilities with duration of up to twelve months. In particular, Management believe that the continued support of its shareholders and access to borrowings from international financial institutions means that the Group would be able to obtain appropriate resources should all liabilities require settlement as disclosed in Note 30. Additionally Group attracted long-term funds in the total amount of AZN 25,819 thousand during March 2011 as disclosed in Note 37.

**Impairment losses on loans and advances.** The Group regularly reviews its loan portfolio to assess impairment. In determining whether an impairment loss should be recorded in the consolidated statement of comprehensive income, the Group makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows.

A 10% increase or decrease in actual loss experience compared to the loss estimates used would result in an increase or decrease in loan impairment losses of AZN 1,244 thousand (2009: AZN 958 thousand), respectively. Impairment losses for individually significant loans are based on estimates of discounted future cash flows of the individual loans, taking into account repayments and realisation of any assets held as collateral against the loans. A 10% increase or decrease in the actual loss experience compared to the estimated future discounted cash flows from individually significant loans, which could arise from differences in amounts and timing of the cash flows, would result in an increase or decrease in loan impairment losses of AZN 785 thousand (2009: AZN 663 thousand), respectively.

**Loans and advances to customers.** The Bank has acquired long term financing from the National Fund for Support of Entrepreneurship of the Republic of Azerbaijan and Mortgage Fund of the Republic of Azerbaijan at interest rates, at which similar organisations ordinarily lend in emerging markets and which may be lower than rates at which the Bank could source the funds from other lenders. As a result of such financing, the Bank was able to issue funds to specific customers at favorable rates. The Group's policy is to recognise financial instruments initially based on their fair values, as required by IAS 39, *Financial Instruments: Recognition and Measurement*. Management has therefore considered whether gains or losses should arise on initial recognition of such instruments. As the transactions are with unrelated parties, management's judgment is that these funds and the related lending are at the market rates and no initial recognition gains or losses should arise.

#### 4 Critical Accounting Estimates and Judgments in Applying Accounting Policies (Continued)

Management have also assessed the nature of the agreement with the Azerbaijan Mortgage Fund, and in particular whether the Bank is acting as an agent of the fund, or as a principal with the borrower under this program. Having considered the risks and rewards related to the loans issued under this program, management have concluded that the Bank is acting as principal and accordingly the accounting in these consolidated financial statements follows this judgement. Had an alternative conclusion been reached, the gross amounts from such loans to customers and due to the Fund, of AZN 22,320 thousand as at 31 December 2010 (2009: AZN 14,025 thousand) would have been excluded from the Group's consolidated financial statements.

**Tax legislation.** Azerbaijani tax, currency and customs legislation is subject to varying interpretations. Refer to Note 33.

**Initial recognition of related party transactions.** In the normal course of business the Group enters into transactions with its related parties. IAS 39 requires initial recognition of financial instruments based on their fair values. Judgement is applied in determining if transactions are priced at market or non-market interest rates, where there is no active market for such transactions. The basis for judgement is pricing for similar types of transactions with unrelated parties and effective interest rate analysis.

#### 5 Adoption of New or Revised Standards and Interpretations

##### (a) Standards effective for annual periods beginning on or after 1 January 2010

The following new standards and interpretations became effective for the Group from 1 January 2010:

**IFRIC 17, Distributions of Non-Cash Assets to Owners** (effective for annual periods beginning on or after 1 July 2009). The interpretation clarifies when and how distribution of non-cash assets as dividends to the owners should be recognised. An entity should measure a liability to distribute non-cash assets as a dividend to its owners at the fair value of the assets to be distributed. A gain or loss on disposal of the distributed non-cash assets should be recognised in profit or loss when the entity settles the dividend payable. IFRIC 17 did not have an impact on these consolidated financial statements.

**IFRIC 18, Transfers of Assets from Customers** (effective for annual periods beginning on or after 1 July 2009). The interpretation clarifies the accounting for transfers of assets from customers, namely, the circumstances in which the definition of an asset is met; the recognition of the asset and the measurement of its cost on initial recognition; the identification of the separately identifiable services (one or more services in exchange for the transferred asset); the recognition of revenue, and the accounting for transfers of cash from customers. IFRIC 18 did not have an impact on these consolidated financial statements.

**IAS 27, Consolidated and Separate Financial Statements** (revised January 2008; effective for annual periods beginning on or after 1 July 2009). The revised IAS 27 requires an entity to attribute total comprehensive income to the owners of the parent and to the non-controlling interests (previously "minority interests") even if this results in the non-controlling interests having a deficit balance (the previous standard required the excess losses to be allocated to the owners of the parent in most cases). The revised standard specifies that changes in a parent's ownership interest in a subsidiary that do not result in the loss of control must be accounted for as equity transactions. It also specifies how an entity should measure any gain or loss arising on the loss of control of a subsidiary. At the date when control is lost, any investment retained in the former subsidiary has to be measured at its fair value. The revised IAS 27 did not have any impact on these consolidated financial statements.

Previously, when the Group ceased to have control or significant influence over an entity, the carrying amount of the investment at the date control or significant influence became its cost for the purposes of subsequently accounting for the retained interests as associates, jointly controlled entity or financial assets. The Group has applied the new accounting policies prospectively to transactions occurring on or after 1 January 2010. As a consequence, no adjustments were necessary to any of the amounts previously recognised in the consolidated financial statements. These revisions did not have an impact on these consolidated financial statements.



**5 Adoption of New or Revised Standards and Interpretations (Continued)**

**IFRS 3, Business Combinations** (revised January 2008; effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009). The revised IFRS 3 allows entities to choose to measure non-controlling interests using the previous IFRS 3 method (proportionate share of the acquiree's identifiable net assets) or at fair value. The revised IFRS 3 is more detailed in providing guidance on the application of the purchase method to business combinations. The requirement to measure at fair value every asset and liability at each step in a step acquisition for the purposes of calculating a portion of goodwill has been removed. Instead, in a business combination achieved in stages, the acquirer has to remeasure its previously held equity interest in the acquiree at its acquisition-date fair value and recognise the resulting gain or loss, if any, in profit or loss for the year. Acquisition-related costs are accounted for separately from the business combination and therefore recognised as expenses rather than included in goodwill. An acquirer has to recognise a liability for any contingent purchase consideration at the acquisition date. Changes in the value of that liability after the acquisition date are recognised in accordance with other applicable IFRSs, as appropriate, rather than by adjusting goodwill. The revised IFRS 3 brings into its scope business combinations involving only mutual entities and business combinations achieved by contract alone. The revised IFRS 3 did not have any impact on these consolidated financial statements.

**Group Cash-settled Share-based Payment Transactions - Amendments to IFRS 2, Share-based Payment** (effective for annual periods beginning on or after 1 January 2010). The amendments provide a clear basis to determine the classification of share-based payment awards in both consolidated and separate financial statements. The amendments incorporate into the standard the guidance in IFRIC 8 and IFRIC 11, which are withdrawn. The amendments expand on the guidance given in IFRIC 11 to address plans that were previously not considered in the interpretation. The amendments also clarify the defined terms in the Appendix to the standard. The amendments did not have a material impact on these consolidated financial statements.

**Eligible Hedged Items—Amendment to IAS 39, Financial Instruments: Recognition and Measurement** (effective with retrospective application for annual periods beginning on or after 1 July 2009). The amendment clarifies how the principles that determine whether a hedged risk or portion of cash flows is eligible for designation should be applied in particular situations. The amendment did not have a material impact on these financial statements. The revised standard did not have a material impact on these consolidated financial statements.

**IFRS 1, First-time Adoption of International Financial Reporting Standards** (following an amendment in December 2008, effective for the first IFRS financial statements for a period beginning on or after 1 July 2009). The revised IFRS 1 retains the substance of its previous version but within a changed structure in order to make it easier for the reader to understand and to better accommodate future changes. The amendments did not have a material impact on these consolidated financial statements.

**Additional Exemptions for First-time Adopters - Amendments to IFRS 1, First-time Adoption of IFRS** (effective for annual periods beginning on or after 1 January 2010). The amendments exempt entities using the full cost method from retrospective application of IFRSs for oil and gas assets and also exempt entities with existing leasing contracts from reassessing the classification of those contracts in accordance with IFRIC 4, 'Determining Whether an Arrangement Contains a Lease' when the application of their national accounting requirements produced the same result. The amendments did not have a material impact on these consolidated financial statements.

**Improvements to International Financial Reporting Standards (issued in April 2009; amendments to IFRS 2, IAS 38, IFRIC 9 and IFRIC 16 are effective for annual periods beginning on or after 1 July 2009; amendments to IFRS 5, IFRS 8, IAS 1, IAS 7, IAS 17, IAS 36 and IAS 39 are effective for annual periods beginning on or after 1 January 2010).** The improvements consist of a mixture of substantive changes and clarifications in the following standards and interpretations: clarification that contributions of businesses in common control transactions and formation of joint ventures are not within the scope of IFRS 2; clarification of disclosure requirements set by IFRS 5 and other standards for non-current assets (or disposal groups) classified as held for sale or discontinued operations; requiring to report a measure of total assets and liabilities for each reportable segment under IFRS 8 only if such amounts are regularly provided to the chief operating decision maker; amending IAS 1 to allow classification of certain liabilities settled by entity's own equity instruments as non-current; changing IAS 7 such that only expenditures that result in a recognised asset are eligible for classification as investing activities; allowing classification of certain long-term land leases as finance leases under IAS 17 even without transfer of ownership of the land at the end of the lease; providing additional guidance in IAS 18 for determining whether an entity acts as a principal or an agent; clarification in IAS 36 that a cash

**5 Adoption of New or Revised Standards and Interpretations (Continued)**

generating unit shall not be larger than an operating segment before aggregation; supplementing IAS 38 regarding measurement of fair value of intangible assets acquired in a business combination; amending IAS 39 (i) to include in its scope option contracts that could result in business combinations, (ii) to clarify the period of reclassifying gains or losses on cash flow hedging instruments from equity to profit or loss for the year and (iii) to state that a prepayment option is closely related to the host contract if upon exercise the borrower reimburses economic loss of the lender; amending IFRIC 9 to state that embedded derivatives in contracts acquired in common control transactions and formation of joint ventures are not within its scope; and removing the restriction in IFRIC 16 that hedging instruments may not be held by the foreign operation that itself is being hedged. In addition, the amendments clarifying classification as held for sale under IFRS 5 in case of a loss of control over a subsidiary published as part of the *Annual Improvements to International Financial Reporting Standards*, which were issued in May 2008, are effective for annual periods beginning on or after 1 July 2009. The amendments did not have a material impact on these consolidated financial statements.

Unless otherwise stated above, the amendments and interpretations did not have any significant effect on the Group's consolidated financial statements.

**(b) Amendments to standards adopted before their effective date**

The Group adopted the amendment to IAS 1, *Presentation of Financial Statements*, which was issued in May 2010 as part of the Annual Improvements to International Financial Reporting Standards. The amendment clarifies the requirements for the presentation and content of the statement of changes in equity. A reconciliation between the carrying amount at the beginning and the end of the period for each component of equity must be presented in the statement of changes in equity, but its content is simplified by allowing an analysis of other comprehensive income by item for each component of equity to be presented in the notes.

**6 New accounting Pronouncements**

Certain new standards and interpretations have been issued that are mandatory for the annual periods beginning on or after 1 January 2011 or later and which the Group has not early adopted.

**Classification of Rights Issues - Amendment to IAS 32** (issued on 8 October 2009; effective for annual periods beginning on or after 1 February 2010). The amendment exempts certain rights issues of shares with proceeds denominated in foreign currencies from classification as financial derivatives.

**Amendment to IAS 24, Related Party Disclosures** (issued in November 2009 and effective for annual periods beginning on or after 1 January 2011). IAS 24 was revised in 2009 by: (a) simplifying the definition of a related party, clarifying its intended meaning and eliminating inconsistencies; and by (b) providing a partial exemption from the disclosure requirements for government-related entities.

**IFRIC 19, Extinguishing Financial Liabilities with Equity Instruments** (effective for annual periods beginning on or after 1 July 2010). This IFRIC clarifies the accounting when an entity renegotiates the terms of its debt with the result that the liability is extinguished through the debtor issuing its own equity instruments to the creditor. A gain or loss is recognised in profit or loss based on the fair value of the equity instruments compared to the carrying amount of the debt.

**Prepayments of a Minimum Funding Requirement – Amendment to IFRIC 14** (effective for annual periods beginning on or after 1 January 2011). This amendment will have a limited impact as it applies only to companies that are required to make minimum funding contributions to a defined benefit pension plan. It removes an unintended consequence of IFRIC 14 related to voluntary pension prepayments when there is a minimum funding requirement.

**Limited exemption from comparative IFRS 7 disclosures for first-time adopters - Amendment to IFRS 1** (effective for annual periods beginning on or after 1 July 2010). Existing IFRS preparers were granted relief from presenting comparative information for the new disclosures required by the March 2009 amendments to IFRS 7, *Financial Instruments: Disclosures*. This amendment to IFRS 1 provides first-time adopters with the same transition provisions as included in the amendment to IFRS 7.

**IFRS 9, Financial Instruments Part 1: Classification and Measurement.** IFRS 9 issued in November 2009 replaces those parts of IAS 39 relating to the classification and measurement of financial assets.

## 6 New accounting Pronouncements (Continued)

IFRS 9 was further amended in October 2010 to address the classification and measurement of financial liabilities. Key features of the standard are as follows:

- Financial assets are required to be classified into two measurement categories: those to be measured subsequently at fair value, and those to be measured subsequently at amortised cost. The decision is to be made at initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument.
- An instrument is subsequently measured at amortised cost only if it is a debt instrument and both (i) the objective of the entity's business model is to hold the asset to collect the contractual cash flows, and (ii) the asset's contractual cash flows represent only payments of principal and interest (that is, it has only "basic loan features"). All other debt instruments are to be measured at fair value through profit or loss.
- All equity instruments are to be measured subsequently at fair value. Equity instruments that are held for trading will be measured at fair value through profit or loss. For all other equity investments, an irrevocable election can be made at initial recognition, to recognise unrealised and realised fair value gains and losses through other comprehensive income rather than profit or loss. There is to be no recycling of fair value gains and losses to profit or loss. This election may be made on an instrument-by-instrument basis. Dividends are to be presented in profit or loss, as long as they represent a return on investment.
- Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The key change is that an entity will be required to present the effects of changes in own credit risk of financial liabilities designated as at fair value through profit or loss in other comprehensive income.

While adoption of IFRS 9 is mandatory from 1 January 2013, earlier adoption is permitted.

**Disclosures—Transfers of Financial Assets – Amendments to IFRS 7 (issued in October 2010 and effective for annual periods beginning on or after 1 July 2011.).** The amendment requires additional disclosures in respect of risk exposures arising from transferred financial assets. The amendment includes a requirement to disclose by class of asset the nature, carrying amount and a description of the risks and rewards of financial assets that have been transferred to another party yet remain on the entity's balance sheet. Disclosures are also required to enable a user to understand the amount of any associated liabilities, and the relationship between the financial assets and associated liabilities. Where financial assets have been derecognised but the entity is still exposed to certain risks and rewards associated with the transferred asset, additional disclosure is required to enable the effects of those risks to be understood.

## 6 New accounting Pronouncements (Continued)

**Improvements to International Financial Reporting Standards (issued in May 2010 and effective from 1 January 2011).** The improvements consist of a mixture of substantive changes and clarifications in the following standards and interpretations: IFRS 1 was amended (i) to allow previous GAAP carrying value to be used as deemed cost of an item of property, plant and equipment or an intangible asset if that item was used in operations subject to rate regulation, (ii) to allow an event driven revaluation to be used as deemed cost of property, plant and equipment even if the revaluation occurs during a period covered by the first IFRS financial statements and (iii) to require a first-time adopter to explain changes in accounting policies or in the IFRS 1 exemptions between its first IFRS interim report and its first IFRS financial statements; IFRS 3 was amended (i) to require measurement at fair value (unless another measurement basis is required by other IFRS standards) of non-controlling interests that are not present ownership interest or do not entitle the holder to a proportionate share of net assets in the event of liquidation, (ii) to provide guidance on acquiree's share-based payment arrangements that were not replaced or were voluntarily replaced as a result of a business combination and (iii) to clarify that the contingent considerations from business combinations that occurred before the effective date of revised IFRS 3 (issued in January 2008) will be accounted for in accordance with the guidance in the previous version of IFRS 3; IFRS 7 was amended to clarify certain disclosure requirements, in particular (i) by adding an explicit emphasis on the interaction between qualitative and quantitative disclosures about the nature and extent of financial risks, (ii) by removing the requirement to disclose carrying amount of renegotiated financial assets that would otherwise be past due or impaired, (iii) by replacing the requirement to disclose fair value of collateral by a more general requirement to disclose its financial effect, and (iv) by clarifying that an entity should disclose the amount of foreclosed collateral held at the reporting date and not the amount obtained during the reporting period; IAS 27 was amended by clarifying the transition rules for amendments to IAS 21, 28 and 31 made by the revised IAS 27 (as amended in January 2008); IAS 34 was amended to add additional examples of significant events and transactions requiring disclosure in a condensed interim financial report, including transfers between the levels of fair value hierarchy, changes in classification of financial assets or changes in business or economic environment that affect the fair values of the entity's financial instruments; and IFRIC 13 was amended to clarify measurement of fair value of award credits. The Group does not expect the amendments to have any material effect on its financial statements, except the amendment to IAS 1 which was early adopted by the Group as explained in Note 5.

New standards issued in May 2011 that are effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted.

IFRS 10 "Consolidated financial statements" replaces all of the guidance on control and consolidation in IAS 27 "Consolidated and separate financial statements" and SIC-12 "Consolidation - special purpose entities". IFRS 10 changes the definition of control so that the same criteria are applied to all entities to determine control.

IFRS 11 "Joint arrangements" replaces IAS 31 "Interests in Joint Ventures" and SIC-13 "Jointly Controlled Entities - Non-Monetary Contributions by Ventures". Changes in the definitions have reduced the "types" of joint arrangements to two: joint operations and joint ventures. The existing policy choice of proportionate consolidation for jointly controlled entities has been eliminated. Equity accounting is mandatory for participants in joint ventures.

IFRS 12 "Disclosure of interest in other entities" applies to entities that have an interest in a subsidiary, a joint arrangement, an associate or an unconsolidated structured entity; it replaces the disclosure requirements currently found in IAS 28 "Investments in associates". IFRS 12 requires entities to disclose information that helps financial statement readers to evaluate the nature, risks and financial effects associated with the entity's interests in subsidiaries, associates, joint arrangements and unconsolidated structured entities. To meet this objective, there is a new requirement to disclose significant judgments and assumptions in determining whether an entity controls, jointly controls or significantly influences its interests in other entities.

As a consequence of above changes IAS 27 is renamed "Separate financial statements". It continues to be a standard dealing solely with separate financial statements. The existing guidance for separate financial statements is unchanged.

IFRS 13 "Fair value measurement" aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across IFRSs.

## **6 New accounting Pronouncements (Continued)**

The Group is currently assessing the impact of the new standards on the consolidated financial statements.

Unless otherwise described above, the new standards and interpretations are not expected to significantly affect the Group's financial statements.

## **7 Cash and Cash Equivalents**

<i>In thousands of Azerbaijani Manats</i>	<b>2010</b>	<b>2009</b>
Cash on hand	26,850	33,240
Cash balances with the CBAR (other than mandatory reserve deposits)	16,821	12,440
Correspondent accounts and overnight placements with other banks		
- The Republic of Azerbaijan	190	163
- Other countries	1,381	2,054
<b>Total cash and cash equivalents</b>	<b>45,242</b>	<b>47,897</b>

Cash balances with the CBAR represent balances on the correspondent account of the Group with the CBAR, which are used by the Group to perform settlements with other banks within the Republic of Azerbaijan. These accounts are non-interest bearing.

Analysis by credit quality of the cash and cash equivalents at 31 December 2010 is as follows:

	<b>Cash balances with the CBAR</b>	<b>Correspondent accounts and overnight placements with other banks</b>	<b>Total</b>
<i>In thousands of Azerbaijani Manats</i>			
<i>Current and not impaired</i>			
- The CBAR	16,821	-	16,821
- Top 15 Azerbaijani banks*	-	34	34
- Other Azerbaijani banks	-	156	156
- OECD banks	-	814	814
- Non-OECD banks	-	567	567
<b>Total current and not impaired</b>	<b>16,821</b>	<b>1,571</b>	<b>18,392</b>
<b>Total cash and cash equivalents (excluding cash on hand)</b>	<b>16,821</b>	<b>1,571</b>	<b>18,392</b>

\* Cash held in top 15 Azerbaijani banks represent the classes of the banks that the management listed in the order from highest to lowest credit quality as used for the purposes of internal monitoring and assessment.

Analysis by credit quality of the cash and cash equivalents at 31 December 2009 is as follows:

**7 Cash and Cash Equivalents (Continued)**

<i>In thousands of Azerbaijani Manats</i>	Cash balances with the CBAR	Correspondent accounts and overnight placements with other banks	Total
<i>Current and not impaired</i>			
- The CBAR	12,440	-	12,440
- Top 15 Azerbaijani banks*	-	87	87
- Other Azerbaijani banks	-	77	77
- OECD banks	-	1,091	1,091
- Non-OECD banks	-	962	962
<b>Total current and not impaired</b>	<b>12,440</b>	<b>2,217</b>	<b>14,657</b>
<b>Total cash and cash equivalents (excluding cash on hand)</b>	<b>12,440</b>	<b>2,217</b>	<b>14,657</b>

Geographical and interest rate analyses of cash and cash equivalents are disclosed in Note 30. The information on related party balances is disclosed in Note 36.

In accordance with the CBAR regulations, the Bank is required to maintain mandatory cash balances with the CBAR calculated as 0.5% (31 December 2009: 0.5%) of the average qualifying customer accounts balances. These mandatory cash balances may be utilised by the Group if the minimum required balance is maintained over the thirty-day reference period (31 December 2009: thirty-day period). The Group has maintained the required level of mandatory reserves throughout the year and subsequently. As at 31 December 2010 and 31 December 2009 none of the mandatory cash balances with the CBAR were overdue.

**8 Due from Other Banks and Financial Institutions**

<i>In thousands of Azerbaijani Manats</i>	2010	2009
Placements with other banks with original maturities of more than three months	5,947	6,980
<b>Total due from other banks and financial institutions</b>	<b>5,947</b>	<b>6,980</b>

Placements with other banks with original maturities of more than three months include placements with resident banks with annual interest rates ranging from 14% p.a. to 20% p.a. (31 December 2009: 15% p.a. to 18% p.a.).



**8 Due from Other Banks and Financial Institutions (Continued)**

Amounts due from other banks are normally collateralised. As at 31 December 2010 fair value of collateral in respect of loans to banks individually determined to be impaired was AZN 2,573 thousand (31 December 2009: AZN 7,050 thousand). However, for impairment provisioning purposes the Group applied a certain level of "haircut" to the fair values of those collaterals as at 31 December 2010 and 31 December 2009.

The analysis by credit quality of amounts due from other banks outstanding at 31 December 2010 is, as follows:

<i>In thousands of Azerbaijani Manats</i>	<b>Placements with other banks with original maturities of more than three months</b>
<i>Current and not impaired</i>	
- Azerbaijani banks (unrated) *	3,674
<b>Total current and not impaired</b>	<b>3,674</b>
<i>Balances individually determined to be impaired (gross)</i>	
- over 360 days overdue	3,411
<b>Total individually impaired (gross)</b>	<b>3,411</b>
Less provision for impairment	(1,138)
<b>Total carrying value of due from other banks and financial institutions</b>	<b>5,947</b>

\* Amounts due from other Azerbaijani banks represent balances with top 25 Azerbaijani banks, which do not have international credit or investment rating

**8 Due from Other Banks and Financial Institutions (Continued)**

The analysis by credit quality of amounts due from other banks outstanding at 31 December 2009 is, as follows:

<i>In thousands of Azerbaijani Manats</i>	<b>Placements with other banks with original maturities of more than three months</b>
<i>Current and not impaired</i>	
- Top 15 Azerbaijan banks	704
- Other Azerbaijani banks (unrated) *	1,363
- Balances renegotiated in 2009	1,800
<b>Total current and not impaired</b>	<b>3,867</b>
<i>Balances individually determined to be impaired (gross)</i>	
- 181 to 360 days overdue	2,395
- over 360 days overdue	3,046
<b>Total individually impaired (gross)</b>	<b>5,441</b>
Less provision for impairment	(2,328)
<b>Total carrying value of due from other banks and financial institutions</b>	<b>6,980</b>

The primary factor that the Group considers whether a deposit is impaired is its overdue status.

The carrying value of each class of amounts due from other banks and financial institutions approximates fair value at 31 December 2010 and 31 December 2009. As at 31 December 2010, the estimated fair value of due from other banks and other financial institutions was AZN 5,947 thousand (31 December 2009: AZN 6,980 thousand). Refer to Note 34.

Geographical, maturity and interest rate analyses of due from other banks and financial institutions are disclosed in Note 30.

Movements in the provision for impairment during 2010 are as follows:

<i>In thousands of Azerbaijani Manats</i>	
<b>Provision for impairment at 1 January 2010</b>	<b>2,328</b>
Reversal of provision for impairment during the year	(1,190)
<b>Provision for impairment at 31 December 2010</b>	<b>1,138</b>

Movements in the provision for impairment during 2009 are, as follows:

<i>In thousands of Azerbaijani Manats</i>	
<b>Provision for impairment at 1 January 2009</b>	<b>550</b>
Provision for impairment during the year	1,778
<b>Provision for impairment at 31 December 2009</b>	<b>2,328</b>

**9 Loans and Advances to Customers**

<i>In thousands of Azerbaijani Manats</i>	<b>2010</b>	<b>2009</b>
Corporate loans	268,517	282,913
Loans to individuals – consumer loans	29,394	42,537
Loans to individuals – entrepreneurs	13,830	19,889
Mortgage loans	87,220	31,431
Less: Provision for loan impairment	(45,514)	(34,261)
<b>Total loans and advances to customers</b>	<b>353,447</b>	<b>342,509</b>

Out of total mortgage loans, AZN 22,320 thousand (31 December 2009: AZN 14,025 thousand) was provided under the programme covered by the borrowing agreement with the Azerbaijan Mortgage Fund, Refer to Note 19. The remaining mortgage loans were covered by the Bank's own resources.

Included in gross loan portfolio is AZN 33,832 thousand accrued interest receivable (31 December 2009: AZN 21,945 thousand)

Movements in the provision for loan impairment during 2010 are as follows:

<i>In thousands of Azerbaijani Manats</i>	<b>Corporate loans</b>	<b>Consumer loans</b>	<b>Individuals – entrepreneurs</b>	<b>Mortgage loans</b>	<b>Total</b>
Provision for loan impairment at 1 January 2010	29,556	3,213	834	658	34,261
Provision for impairment during the year	8,314	595	3,066	715	12,690
Amounts written off during the period as uncollectible	(1,437)	-	-	-	(1,437)
<b>Provision for loan impairment at 31 December 2010</b>	<b>36,433</b>	<b>3,808</b>	<b>3,900</b>	<b>1,373</b>	<b>45,514</b>

Movements in the provision for loan impairment during 2009 are as follows:

<i>In thousands of Azerbaijani Manats</i>	<b>Corporate loans</b>	<b>Consumer loans</b>	<b>Individuals – entrepreneurs</b>	<b>Mortgage loans</b>	<b>Total</b>
Provision for loan impairment at 1 January 2009	21,350	2,357	548	422	24,677
Provision for impairment during the year	8,206	856	286	236	9,584
<b>Provision for loan impairment at 31 December 2009</b>	<b>29,556</b>	<b>3,213</b>	<b>834</b>	<b>658</b>	<b>34,261</b>

**9 Loans and Advances to Customers (Continued)**

Economic sector risk concentrations within the customer loan portfolio are as follows:

<i>In thousands of Azerbaijani Manats</i>	2010		2009	
	Amount	%	Amount	%
<i>Loans to individuals:</i>				
- Consumer loans	32,624	8	42,537	11
- Entrepreneurship	13,830	3	19,889	5
- Mortgage	87,220	22	31,431	9
<b>Total loans to individuals</b>	<b>133,674</b>	<b>34</b>	<b>93,857</b>	<b>25</b>
<i>Corporate loans:</i>				
- Trade	68,678	17	77,652	21
- Services	9,996	3	14,697	4
- Construction	59,119	15	75,839	20
- Manufacturing	76,442	19	87,583	23
- Agricultural	29,466	7	10,928	3
- Transport and communication	21,586	5	16,209	4
- Other	-	-	5	-
<b>Total corporate loans</b>	<b>265,287</b>	<b>66</b>	<b>282,913</b>	<b>75</b>
<b>Total loans and advances to customers (before impairment)</b>	<b>398,961</b>	<b>100%</b>	<b>376,770</b>	<b>100</b>

At 31 December 2010, the Group had 61 borrowers (2009: 84 borrowers) with aggregated loan amounts above AZN 1,000 thousand. The total aggregate amount of these loans was AZN 150,614 thousand (2009: AZN 213,617 thousand) or 38% of the gross loan portfolio (2009: 57%).

Information about collateral at 31 December 2010 is as follows:

<i>In thousands of Azerbaijani Manats</i>	Corporate	Loans to	Loans to	Mortgage	Total
Unsecured loans		10,732			
Loans collateralised by:					
- movable property	201,973	8,949	10,333	37,749	259,004
- tradable securities	13,559	3,998	25	254	17,836
- cash deposits	7,635	-	-	1,379	9,014
- other assets	589	5,408	-	60	6,057
- guarantees	9,756	306	454	-	10,516
	-	-	-	43,385	43,385
<b>Total loans and advances to customers</b>	<b>268,519</b>	<b>29,393</b>	<b>13,829</b>	<b>87,220</b>	<b>398,961</b>

**9 Loans and Advances to Customers (Continued)**

Information about collateral at 31 December 2009 is as follows:

<i>In thousands of Azerbaijani Manats</i>	Corporate loans	Loans to individuals – consumer loans	Loans to individuals – entrepreneurs	Mortgage loans	Total
Unsecured loans	39,524	17,532	3,266	2,337	62,659
Loans collateralised by:					
- real estate	198,209	15,784	16,067	26,041	256,101
- movable property	-	4,819	-	-	4,819
- tradable securities	10,816	4,299	303	234	15,652
- cash deposits	26,571	-	-	2,685	29,256
- other assets	7,793	103	253	134	8,283
<b>Total loans and advances to</b>	<b>282,913</b>	<b>42,537</b>	<b>19,889</b>	<b>31,431</b>	<b>376,770</b>

The analysis by credit quality of loans outstanding at 31 December 2010 is as follows:

<i>In thousands of Azerbaijani Manats</i>	Corporate loans	Consumer loans	Individuals - entrepreneurs	Mortgage loans	Total
<i>Current and not impaired</i>					
Unsecured loans	33,124	7,421	1,761	2,550	44,856
Loans collateralised by:					
- real estate	136,055	5,500	5,467	35,186	182,208
- movable property	9,566	2,485	236	213	12,500
- tradable securities	5,762	-	-	1,068	6,830
- cash deposits	13	5,156	-	60	5,229
- other assets	9,557	280	1	42,703	52,541
<b>Total current and not impaired</b>	<b>194,077</b>	<b>20,842</b>	<b>7,465</b>	<b>81,780</b>	<b>304,164</b>
<i>Past due, but not impaired</i>					
- less than 30 days overdue	2,399	1,767	-	736	4,902
- 30 to 90 days overdue	12,209	1,241	111	1,458	15,019
- 90 to 180 days overdue	1,445	1,443	235	737	3,860
- 180 to 360 days overdue	3,105	724	7	207	4,043
- over 360 days overdue	4,211	505	878	519	6,113
<b>Total past due but not impaired</b>	<b>23,369</b>	<b>5,680</b>	<b>1,231</b>	<b>3,657</b>	<b>33,937</b>
<i>Loans individually determined to be</i>					
- less than 30 days overdue	1,060	513	318	301	2,192
- 30 to 90 days overdue	573	351	158	95	1,177
- 90 to 180 days overdue	632	832	241	55	1,760
- 180 to 360 days overdue	23,323	972	142	715	25,152
- over 360 days overdue	24,486	1,158	4,320	615	30,579
<b>Total individually impaired loans</b>	<b>50,074</b>	<b>3,826</b>	<b>5,179</b>	<b>1,781</b>	<b>60,860</b>
<b>Gross carrying value of loans</b>	<b>267,520</b>	<b>30,348</b>	<b>13,875</b>	<b>87,218</b>	<b>398,961</b>
<b>Less impairment provisions</b>	<b>(36,433)</b>	<b>(3,808)</b>	<b>(3,900)</b>	<b>(1,373)</b>	<b>(45,514)</b>
<b>Total loans and advances to customers</b>	<b>231,087</b>	<b>26,540</b>	<b>9,975</b>	<b>85,845</b>	<b>353,447</b>

**9 Loans and Advances to Customers (Continued)**

The analysis by credit quality of loans outstanding at 31 December 2009 is as follows:

	Corporate loans	Loans to individuals – consumer loans	Loans to individuals – entrepreneurs	Mortgage loans	Total
<i>In thousands of Azerbaijani Manats</i>					
<i>Current and not impaired</i>					
Unsecured loans	35,042	15,739	3,215	2,337	56,333
Loans collateralised by:					
- real estate	164,200	13,886	15,168	25,917	219,171
- movable property	7,318	3,582	203	234	11,337
- tradable securities	18,006	-	-	2,685	20,691
- cash deposits	-	4,819	-	-	4,819
- other assets	7,794	103	-	134	8,031
<b>Total current and not impaired</b>	<b>232,360</b>	<b>38,129</b>	<b>18,586</b>	<b>31,307</b>	<b>320,382</b>
<i>Past due, but not impaired</i>					
- less than 30 days overdue	18,268	694	447	18	19,427
- 30 to 90 days overdue	1,942	674	115	2	2,733
- 90 to 180 days overdue	847	470	105	17	1,439
- 180 to 360 days overdue	3,306	1,229	430	7	4,972
- over 360 days overdue	7,756	866	166	80	8,868
<b>Total past due but not impaired</b>	<b>32,119</b>	<b>3,933</b>	<b>1,263</b>	<b>124</b>	<b>37,439</b>
<i>Loans individually determined to be impaired (gross)</i>					
- less than 30 days overdue	4,449	49	14	-	4,512
- 30 to 90 days overdue	9	53	-	-	62
- 90 to 180 days overdue	733	275	-	-	1,008
- 180 to 360 days overdue	6,923	56	6	-	6,985
- over 360 days overdue	6,320	42	20	-	6,382
<b>Total individually impaired loans (gross)</b>	<b>18,434</b>	<b>475</b>	<b>40</b>	<b>-</b>	<b>18,949</b>
<b>Gross carrying value of loans</b>	<b>282,913</b>	<b>42,537</b>	<b>19,889</b>	<b>31,431</b>	<b>376,770</b>
<b>Less impairment provisions</b>	<b>(29,556)</b>	<b>(3,213)</b>	<b>(834)</b>	<b>(658)</b>	<b>(34,261)</b>
<b>Total loans and advances to customers</b>	<b>253,357</b>	<b>39,324</b>	<b>19,055</b>	<b>30,773</b>	<b>342,509</b>

The Group applied the portfolio provisioning methodology prescribed by IAS 39, *Financial Instruments: Recognition and Measurement*, and created portfolio provisions for impairment losses that were incurred but have not been specifically identified with any individual loan by the end of the reporting period. The Group's policy is to classify each loan as 'current and not impaired' until a specific objective evidence of impairment of the loan is identified. Included in "Current and not impaired" loans as at 31 December 2009 are loans renegotiated during 2010 in the amount of AZN 105,113 thousand (2009: AZN 120,685 thousand).

The primary factors that the Group considers whether a loan is impaired is its overdue status and realisability of related collateral, if any. The Group presents above an ageing analysis of loans that are individually determined to be impaired.



**9 Loans and Advances to Customers (Continued)**

Current and not impaired, but renegotiated loans, represent the carrying amount of loans that would otherwise be past due or impaired whose terms have been renegotiated. Past due but not impaired loans represent collateralised loans where the fair value of collateral covers the overdue interest and principal repayments. The amount reported as past due, but not impaired is the whole balance of such loans, not only the individual instalments that are past due.

Fair value of collateral in respect of loans past due but not impaired and in respect of loans individually determined to be impaired at 31 December 2010 was as follows:

	Corporate loans	Loans to individuals – consumer loans	Loans to individuals – entrepreneurs	Mortgage loans	Total
<i>In thousands of Azerbaijani Manats</i>					
<i>Fair value of collateral - loan past due but not impaired</i>					
- real estate	25,307	3,228	2,862	1,778	33,175
- movable property	421	-	-	792	1,213
- tradable securities	115	1,383	-	36	1,534
- other assets	91	-	-	412	503
<i>Fair value of collateral - individually impaired loans</i>					
- real estate	53,862	2,540	4,863	1,912	63,177
- movable property	1,571	1,108	-	-	2,679
- other assets	-	-	-	57	57
<b>Total</b>	<b>81,367</b>	<b>8,259</b>	<b>7,725</b>	<b>4,987</b>	<b>102,338</b>

Fair value of collateral in respect of loans past due but not impaired and in respect of loans individually determined to be impaired at 31 December 2009 was as follows:

	Corporate loans	Loans to individuals – consumer loans	Loans to individuals – entrepreneurs	Mortgage loans	Total
<i>In thousands of Azerbaijani Manats</i>					
<i>Fair value of collateral - loan past due but not impaired</i>					
- real estate	32,619	3,234	1,639	410	37,902
- movable property	2,715	1,055	246	-	4,016
- tradable securities	11,228	-	-	-	11,228
<i>Fair value of collateral - individually impaired loans</i>					
- real estate	15,339	242	40	-	15,621
- movable property	2,216	214	-	-	2,430
<b>Total</b>	<b>64,117</b>	<b>4,745</b>	<b>1,925</b>	<b>410</b>	<b>71,197</b>

**9 Loans and Advances to Customers (Continued)**

The fair value of real estate and other assets was determined by the Group's credit department, using the Group's internal guidelines. These internal guidelines prescribe the basis that fair values are determined based on available market information (for example, related to recent transactions involving similar properties) and the need to consult with third party valuers to the extent that information on fair values is not readily ascertainable.

The carrying value of each class of loans and advances to customers approximates fair value at 31 December 2010 and 31 December 2009. At 31 December 2010, the estimated fair value of loans and advances to customers was AZN 353,447 thousand (2009: AZN 342,509 thousand). Refer to Note 34.

The interest rate analysis of loans and advances to customers is disclosed in Note 30. The information on related party balances is disclosed in Note 36.

**10 Investment Securities Available for Sale**

<i>In thousands of Azerbaijani Manats</i>	<b>2010</b>	<b>2009</b>
Corporate shares – unquoted	853	609
<b>Total investment securities available for sale</b>	<b>853</b>	<b>609</b>

The movements in investment securities available for sale are as follows:

<i>In thousands of Azerbaijani Manats</i>	<b>2010</b>	<b>2009</b>
Carrying amount at 1 January	609	550
Acquisition of investment securities available for sale	275	-
Revaluation	(31)	59
<b>Carrying amount at 31 December</b>	<b>853</b>	<b>609</b>

Equity investment securities available for sale are:

<b>Name</b>	<b>Nature of business</b>	<b>Country of registration</b>	<b>Carrying value</b>	
			<b>2010</b>	<b>2009</b>
Milli Kart	Plastic card operator	Azerbaijan	400	400
Baku Stock Exchange	Financial services	Azerbaijan	60	60
Visa Inc.	Clearing house	USA	118	149
Other	Miscellaneous	Other	275	-
<b>Total</b>			<b>853</b>	<b>609</b>

The investment in Baku Stock Exchange was made in 2006 and represents 5.6% of its total share capital. Currently the stock market in the Republic of Azerbaijan is practically non-existent, and the activity of Baku Stock Exchange as at the reporting date is still limited. However, management of the Group believes that the fair value of this investment does not differ materially from its carrying value (which is its cost).

The investment in Milli Kart was made in 2006 and represents 10% of its total share capital. Management of the Group believes that the fair value of this investment does not differ materially from its carrying value.

These securities are not actively traded in the stock market. Transactions occur from time to time between existing shareholders at nominal values of the shares.

The investment in Visa Inc. was made in 2008, number of shares 2,131 with a nominal value of 42 AZN.

Investment in other companies consists of 11 small foreign companies whose number change constantly. The account mainly includes the small portion of shares in foreign companies with various business backgrounds.

## **11 Other Investment Securities**

<i>In thousands of Azerbaijani Manats</i>	<b>2010</b>	<b>2009</b>
Mortgage Fund Notes	-	2,186
Accord Inshaat-Sanaye OJSC bonds	11,847	-
Other non government notes	1,132	150
<b>Total other investment securities</b>	<b>12,979</b>	<b>2,336</b>

On October and December 2009 Group obtained Mortgage Fund notes in amount of AZN 2,186 thousand. The interest rate was 3% p.a. and they were paid back during 2010.

On November 2010 Group obtained Accord Inshaat-Senaye OJSC bonds in amount of AZN 11,847 thousand. The interest rate is 3% p.a. with a maturity in November 2011.

Management could not reliably estimate the fair value of the securities. These securities are not actively traded in the stock market. The notes are carried at amortised cost.

During 2010 Group obtained non government notes in amount of AZN 1,132 thousand. These notes mainly include the small portion of notes in foreign and local companies.

## **12 Investment Properties**

<i>In thousands of Azerbaijani Manats</i>	<b>Note</b>	<b>2010</b>	<b>2009</b>
<b>Investment properties at fair value as at 1 January</b>		<b>1,181</b>	<b>253</b>
Acquisition of new investment property		15,651	-
Transfer to owner occupied premises		(554)	-
Transfer from owner occupied premises	13	-	817
Fair value gains/(losses)		-	111
<b>Investment properties at fair value as at 31 December</b>		<b>16,278</b>	<b>1,181</b>

The Group acquired new investment property in Khatai district during 2010 amounting to AZN 15,651 thousand, for capital appreciation purposes.

During 2010, the Group rented out 200 square metres (2009: nil square metres) of its new investment property which is situated in Narimanov district and 284 square metres (2009: 284 square metres) of its Mingechevir branch.

The rental income on investment property in 2010 amounted to AZN 28 thousand (2009: AZN 20 thousand) and is included in other operating income.

The Group did not classify any operating leases as investment properties. Investment property was independently valued at 31 December 2009. The valuation was carried out by an independent firm of valuers, REC - INVEST, who hold a recognised and relevant professional qualification and who have recent experience in valuation of assets of similar location and category. The basis used for the appraisal was market value. Management believes that there was no significant change in the fair value of investment property since 31 December 2009.

**Technikabank OJSC**

**Notes to the Consolidated Financial Statements – 31 December 2010**

**13 Premises, Equipment and Intangible Assets**

*In thousands of Azerbaijani Manats*

	Note	Premises	Office and computer equipment	Motor vehicles	Construction in Progress	Total premises and equipment	Computer software licences	Total
Cost or valuation at 1 January 2009		29,125 (730)	7,483 (2,395)	1,605 (741)	2,400 -	40,613 (3,866)	1,320 (69)	41,933 (3,935)
Accumulated depreciation/amortisation								
<b>Carrying amount at 1 January 2009</b>		<b>28,395</b>	<b>5,088</b>	<b>864</b>	<b>2,400</b>	<b>36,747</b>	<b>1,251</b>	<b>37,998</b>
Additions		4,442	3,109 (92)	101	-	7,652 (92)	864	8,516
Transfers from computer software licenses		-	156	-	-	-	92	-
Transfers from CIP		2,244 (817)	-	-	(2,400)	-	-	-
Transfer to Investment property	12	-	-	-	-	(817)	-	(817)
Acquisition through business combinations		-	835	-	-	835	579	1,414
Acquisition through business combinations - accumulated depreciation		-	(355)	-	-	(355)	(100)	(455)
Disposals		-	(471)	-	-	(471)	-	(471)
Disposed accumulated depreciation		-	431	-	-	431	-	431
Depreciation/amortisation charge	26	(1,039)	(1,893)	(344)	-	(3,276)	(58)	(3,334)
Revaluation – Cost		(3,259)	-	-	-	(3,259)	-	(3,259)
Revaluation – Accumulated Depreciation		1,716	-	-	-	1,716	-	1,716
<b>Carrying amount at 31 December 2009</b>		<b>31,682</b>	<b>6,808</b>	<b>621</b>	<b>-</b>	<b>39,111</b>	<b>2,628</b>	<b>41,739</b>
Cost or valuation at 31 December 2009		31,735 (53)	11,020 (4,212)	1,706 (1,085)	-	44,461 (5,350)	2,855 (227)	47,316 (5,577)
Accumulated depreciation/amortisation								
<b>Carrying amount at 31 December 2009</b>		<b>31,682</b>	<b>6,808</b>	<b>621</b>	<b>-</b>	<b>39,111</b>	<b>2,628</b>	<b>41,739</b>
Additions		109	1,903	614	260	2,886	1,574	4,460
Transfer from investment property	12	554	-	-	-	554	-	554
Transfer to other assets	15	-	-	-	-	-	(1,698)	(1,698)
Disposals		-	(1,284)	(120)	-	(1,404)	(73)	(1,477)
Disposed accumulated depreciation		-	1,225	120	-	1,345	73	1,418
Depreciation/amortisation charge	26	(1,004)	(2,395)	(391)	-	(3,790)	(261)	(4,051)
<b>Carrying amount at 31 December 2010</b>		<b>31,341</b>	<b>6,257</b>	<b>844</b>	<b>260</b>	<b>38,702</b>	<b>2,243</b>	<b>40,945</b>
Cost or valuation at 31 December 2010		32,398 (1,057)	11,639 (5,382)	2,200 (1,356)	260 -	46,497 (7,795)	2,658 (415)	49,155 (8,210)
Accumulated depreciation/amortisation								
<b>Carrying amount at 31 December 2010</b>		<b>31,341</b>	<b>6,257</b>	<b>844</b>	<b>260</b>	<b>38,702</b>	<b>2,243</b>	<b>40,945</b>

### 13 Premises, Equipment and Intangible Assets (Continued)

Premises were independently valued at 31 December 2009. The valuation was carried out by an independent firm of valuers, REC - INVEST. The basis used for the appraisal was market value. Fair values were estimated, using appropriate valuation techniques under the assumption that observable prices in an active market for the premises of characteristics and locations similar to those of the Group's premises do not differ significantly from, and, therefore, are a good indication of the fair value of the Group's premises. As a result of the valuation, the net carrying amount of buildings decreased by AZN 1,542 thousand. Revaluation increase through revaluation reserve of AZN 793 thousand and revaluation decrease of AZN 2,335 thousand through comprehensive income relating to revaluation of buildings of the Bank were recorded. There was no valuation carried out since 31 December 2009, management believes that there was no significant change in market value of premises since last valuation performed at 31 December 2009.

The realised portion of revaluation reserve on buildings in the amount of AZN 94 thousand (2009: AZN 80 thousand) was transferred to retained earnings due to depreciation of revalued buildings.

### 14 Other Financial Assets

<i>In thousands of Azerbaijani Manats</i>	2010	2009	2008
Restricted cash	1,624	2,204	276
Receivables from shareholders	1,197	-	-
Fee and commission receivable	373	669	475
Settlements with operators of payment systems	839	341	477
Credit and debit cards-related receivables	-	46	331
Other receivables	122	-	-
<b>Total other financial assets</b>	<b>4,155</b>	<b>3,260</b>	<b>1,559</b>

Restricted cash balances represent security deposits placed with two resident banks to ensure rendering of plastic cards processing services, as well as a guarantee deposit placed with a payment system operator. The Group does not have the right to use these funds for the purposes of funding its own activities. Refer to Note 3

Receivables from shareholders represent withholding tax paid by the Group on shareholders' behalf and will unconditionally be collected from the shareholders. Refer to Note 36.

The analysis by credit quality of other financial assets at 31 December 2010 is, as follows:

<i>In thousands of Azerbaijani Manats</i>	Restricted cash	Receivables from shareholders	Fee and commission receivable	Settlements with operators of payment systems	Other receivables	Total
<i>Current and not impaired</i>						
- Azerbaijan	-	1,197	373	-	122	1,692
- OECD	1,624	-	-	331	-	1,955
- Non OECD	-	-	-	508	-	508
<b>Total current and not impaired</b>	<b>1,624</b>	<b>1,197</b>	<b>373</b>	<b>839</b>	<b>122</b>	<b>4,155</b>

## 14 Other Financial Assets (Continued)

The analysis by credit quality of amounts outstanding at 31 December 2009 is as follows:

<i>In thousands of Azerbaijani Manats</i>	Restricted cash	Fee and commission receivable	Settlements with operators of payment systems	Other receivables	Total
<i>Current and not impaired</i>					
- Azerbaijan	-	669	-	46	715
- OECD	1,835	-	-	-	1,835
- Non OECD	369	-	341	-	710
<b>Total current and not impaired</b>	<b>2,204</b>	<b>669</b>	<b>341</b>	<b>46</b>	<b>3,260</b>

The primary factors that the Group considers whether a receivable is impaired is its overdue status and realisability of related collateral, if any.

The carrying value of each class of other financial assets approximates fair value at 31 December 2010 and 31 December 2009. Refer to Note 34. Geographical and maturity analyses of other financial assets are disclosed in Note 30.

## 15 Other Assets

<i>In thousands of Azerbaijani Manats</i>	2010	2009	2008
Prepayments for other services	261	315	280
Reposessed asset	749	-	-
Insurance premium receivable	332	80	290
Reinsurers' share of reserve for unearned premiums	175	457	546
Prepayment for other taxes	12	111	-
Prepayments for purchase of premises and equipment / intangible assets	5,766	1,237	1,207
Prepayments to suppliers for lease equipment	-	512	1,827
Gold	1,362	-	-
Other	123	146	180
<b>Total other assets</b>	<b>8,780</b>	<b>2,858</b>	<b>4,330</b>
Current assets	3,014	1,109	1,296
Non-current assets	5,766	1,749	3,034

The Group made prepayments for the purchase of intangible assets (banking software) during the years ended 31 December 2010 and 31 December 2009. Those prepayments were classified as Intangible Assets as at 31 December 2009 and was reclassified to Other Assets at 31 December 2010 (under "prepayments for purchase of premises and equipment/intangible assets"). Management believes that before the implementation of this software, it should not be classified as intangible assets. This asset has not been amortised during the aforementioned periods. As a result of this reclassification, management presented the Statement of Financial Position as at 31 December 2008, as well. Refer to Note 13.

Prepayments for purchase of premises and equipment also include advance payment in the amount of AZN 3,854 thousand made by one of the subsidiaries of the Group Technikaleasing LLC for premises to be acquired in 2011.

During 2010 the Group acquired the gold shares, which represent fractional, undivided interests in the Trust, the primary asset of which is allocated gold.

Gold shares are listed on the NYSE Arca and trade the same way ordinary stocks do. The gold bullion is held by the Custodian, HSBC Bank USA, in its London vault.

## **16 Due to Other Banks and Financial Institutions**

<i>In thousands of Azerbaijani Manats</i>	<b>2010</b>	<b>2009</b>
Correspondent accounts and overnight placements of other banks	4,723	6,144
Short - term placements of other banks	17,102	22,612
Long - term placements of other banks	73	70
<b>Total due to other banks and financial institutions</b>	<b>21,898</b>	<b>28,826</b>

The carrying value of each class of due to other banks and financial institutions approximates fair value at 31 December 2010 and 31 December 2009. As at 31 December 2010, the estimated fair value of due to other banks was AZN 21,898 thousand (31 December 2009: AZN 28,826 thousand). Refer to Note 34.

Placements of other banks include placements of resident and non resident banks and financial institutions with annual interest rates ranging from 3% to 16% (2009: 6% to 16%) and maturities from January 2011 to December 2015.

At 31 December 2010, 5 banks had balances with the Group (2009: 4 banks) with aggregated amounts above AZN 1,500 thousand. The total aggregate amount of these deposits was AZN 20,412 thousand (2009: AZN 24,103 thousand) or 93% of the total amount due to other banks and financial institutions (2009: 84%).

Geographical, maturity and interest rate analyses of due to other banks are disclosed in Note 30.

## **17 Customer Accounts**

<i>In thousands of Azerbaijani Manats</i>	<b>2010</b>	<b>2009</b>
<b>State and public organisations</b>		
- Current/settlement accounts	12,275	14,036
- Term deposits	232	315
<b>Other legal entities</b>		
- Current/settlement accounts	44,553	50,397
- Term deposits	27,958	10,430
<b>Individuals</b>		
- Current/settlement accounts	27,925	19,281
- Term deposits	158,443	95,353
<b>Total customer accounts</b>	<b>271,386</b>	<b>189,812</b>

**17 Customer Accounts (Continued)**

Economic sector concentrations within customer accounts are as follows:

<i>In thousands of Azerbaijani Manats</i>	2010		2009	
	Amount	%	Amount	%
Individuals	186,368	69	114,634	60
Trade	20,752	8	22,073	12
Transportation and communication	4,593	2	14,854	8
Real estate	17,848	7	14,577	8
State and public organisations*	10,182	4	4,503	2
Manufacturing	13,640	5	8,947	5
Energy	3,353	1	3,743	2
Agriculture	290	-	403	-
Other	14,360	5	6,078	3
<b>Total customer accounts</b>	<b>271,386</b>	<b>100</b>	<b>189,812</b>	<b>100</b>

(\*) State and public organisations comprise ministries, Treasury, municipalities and other state bodies of the Republic of Azerbaijan, excluding profit making state and public organisations that are included in the respective categories.

The carrying value of each class of customer accounts approximates fair value at 31 December 2010 and 31 December 2009. At 31 December 2010, the estimated fair value of customer accounts was AZN 271,386 thousand (31 December 2009: AZN 189,812 thousand). Refer to Note 34.

Geographical, maturity and interest rate analyses of customer accounts are disclosed in Note 30. The information on related party balances is disclosed in Note 36.

At 31 December 2010, the Group had 26 customers (31 December 2009: 30 customers) with balances above AZN 1,000 thousand. The aggregate balance of these customers was AZN 67,993 thousand (31 December 2009: AZN 83,648 thousand) or 26% (31 December 2009: 44%) of total customer accounts.

**18 Debt Securities in Issue**

<i>In thousands of Azerbaijani Manats</i>	2010	2009
Debentures	3,337	10,906
<b>Total debt securities in issue</b>	<b>3,337</b>	<b>10,906</b>

On 14 March 2007, the Group issued 2,000 corporate debentures through a primary placement at the Baku Stock Exchange, with a par value of AZN 1,000 each. These debentures are denominated in AZN, bear interest at a rate of 14% p.a. and mature on 12 March 2012. These debentures were sold on the issue date to a foreign investment fund company registered in the Cayman Islands and domiciled in the Russian Federation. These debentures with the total amount of AZN 2,000 thousand have been purchased by Kazimir Growth and Kazimir Master Funds; both affiliated with Kazimir Caspian Fund Limited, a 10% shareholder of the Bank. Refer to Note 36. The outstanding amount of debentures in issue including the accrued interest payable was AZN 2,083 thousand as at 31 December 2010 (31 December 2009: AZN 2,083 thousand).

On 15 March 2007, the Group issued 1,000 corporate debentures through a primary placement at the Baku Stock Exchange, with a par value of USD 1,000 each. These debentures are denominated in USD, bear interest rate of 15% p.a. and mature on 22 November 2012. The outstanding amount of debentures in issue including the accrued interest payable was AZN 831 thousand as at 31 December 2010 (31 December 2009: AZN 838 thousand).



**18 Debt Securities in Issue (continued)**

On 15 August 2008, the Group issued 100,000 corporate debentures through a primary placement at the Baku Stock Exchange, with par value of USD 100 each. These debentures are denominated in USD and have an effective interest rate of 15,83% p.a and mature on 15 August 2011. These debentures were sold on the issue date to a foreign bank - "Parex Bank" (Arranger). Note holders had the right to demand repayment of Principal on 15 February 2010. Put option right was used by most of the Note holders; Group repaid USD 9,804 thousand in February 2010. The outstanding amount of debentures in issue including the accrued interest payable was AZN 423 thousand as at 31 December 2010 (31 December 2009: AZN 7,985 thousand).

The carrying value of debt securities approximates fair value at 31 December 2010 and 31 December 2009. As at 31 December 2010, the estimated fair value of debt securities was AZN 3,337 thousand (31 December 2009: AZN 10,906 thousand). The interest rate analysis of debt securities in issue is disclosed in Note 30. The information on debt securities in issue held by related parties is disclosed in Note 36.

**19 Term Borrowings from Other Banks and Financial Institutions**

<i>In thousands of Azerbaijani Manats</i>	<b>2010</b>	<b>2009</b>
Term borrowings from the CBAR	60,284	100,418
Term borrowings from National Fund for Financial Aid to Entrepreneurs	26,046	27,328
Term borrowings from National Mortgage Fund	22,320	14,025
Term borrowings from Ministry of Agriculture	10,604	10,419
Term borrowings from Black Sea Trade and Development	3,715	4,817
<b>Total term borrowings from other banks and financial institutions</b>	<b>122,969</b>	<b>157,007</b>

The interest rate on funds borrowed from the CBAR is 2% - 3% (31 December 2009: 2% and 3%) per annum. These borrowings mature between February 2011 and August 2020. There are no financial covenant requirements applicable to these borrowings.

On 5 May 2005 and on 17 February 2006, the Group signed credit agreement with the National Fund for Support of Entrepreneurship, a programme under the auspices of the Ministry for Economic Development of the Republic of Azerbaijan, for financing of small and medium size enterprises. Under this programme, funds are made available to the Group at an interest rate of 1%-2% and 2% respectively per annum and the Group further on lends these funds to eligible borrowers at rates not higher than 7%-8% and 5%-8% respectively per annum. These borrowings mature between June 2011 and December 2021. There are no financial covenant requirements applicable to these borrowings.

On 4 September 2007, the Group signed an agreement with the Ministry of Agriculture of the Republic of Azerbaijan for financing of agricultural projects. Under this programme, funds are made available to the Group at an interest rate of 2% per annum and the Group further on lends these funds to eligible borrowers at rates not higher than 7% per annum. There are no financial covenant requirements applicable to these borrowings.

On 6 December 2007, the Group signed credit agreement with Black Sea Trade and Development Bank, registered in the Republic of Greece, for a total of USD 8,000 thousand for financing mortgage loans. These borrowings bear interest of 6 month LIBOR plus 3.7% per annum and mature in December 2013. The Group is obliged to comply with certain financial covenants stipulated by the loan agreement. As at 31 December 2010, the Group was not in compliance with certain financial covenants specified in this loan agreement. For information on covenants related to these borrowings refer to Note 33.

The carrying value of each class of term borrowings from other banks and other financial institutions approximates fair value at 31 December 2010 and 31 December 2009. As at 31 December 2010, the estimated fair value of term borrowings from other banks and financial institutions was AZN 122,969 thousand (31 December 2009: AZN 157,007 thousand). For information on the fair value of term borrowings from other banks and other financial institutions refer to Note 34.

Geographical, maturity and interest rate analyses of term borrowings from other banks and financial institutions are disclosed in Note 30.

## 20 Other Financial Liabilities

Other financial liabilities comprise the following:

<i>In thousands of Azerbaijani Manats</i>	2010	2009
Amounts in the course of settlement	394	673
Payable to supplier of lease equipment	-	508
Trade payables	208	466
Other payables	-	93
<b>Total other financial liabilities</b>	<b>602</b>	<b>1,740</b>

All other financial liabilities represent current liabilities as at 31 December 2010 and 31 December 2009.

Carrying value of each class of other financial liabilities approximates fair value at 31 December 2010 and 31 December 2009. At 31 December 2010 the estimated fair value of other financial liabilities was AZN 602 thousand (2009: AZN 1,740 thousand). For information on the fair value of other financial liabilities refer to Note 34.

## 21 Other Liabilities

Other liabilities comprise the following:

<i>In thousands of Azerbaijani Manats</i>	2010	2009
Unearned insurance premiums reserve (UPR)	1,396	1,448
Outstanding claims reserve	-	25
Advances received from customers for lease equipment	-	403
Property tax payable	167	165
Taxes other than on income	71	-
Payable to deposit insurance fund	162	-
Other	27	132
<b>Total other liabilities</b>	<b>1,823</b>	<b>2,173</b>
Current	502	-
Non-current	1,321	2,173

The movement in the unearned premiums reserve is shown below:

<i>In thousands of Azerbaijani Manats</i>	1 January 2009	Increase/(decrease) during the year	31 December 2009	Increase/(decrease) during the year	31 December 2010
<b>IBNR</b>					
Gross	-	144	144	(137)	7
Reinsurer's share	-	(17)	(17)	14	(3)
<b>Net</b>	-	127	127	(123)	4
<b>UPR</b>					
Gross	1,726	(422)	1,304	85	1,389
Reinsurer's share	(546)	106	(440)	268	(172)
<b>Net</b>		(316)	864	353	1,217
<b>Total</b>	<b>1,180</b>	<b>(189)</b>	<b>991</b>	<b>230</b>	<b>1,221</b>

## 22 Share Capital

<i>In thousands of AZN except for number of shares</i>	<b>Number of outstanding shares</b>	<b>Ordinary shares</b>	<b>Share premium</b>	<b>Total</b>
<b>At 1 January 2009</b>	<b>26,912</b>	<b>26,912</b>	<b>3,464</b>	<b>30,376</b>
New shares issued	14,800	14,800	-	14,800
<b>At 31 December 2009</b>	<b>41,712</b>	<b>41,712</b>	<b>3,464</b>	<b>45,176</b>
New shares issued	11,973	11,973	-	11,973
<b>At 31 December 2010</b>	<b>53,685</b>	<b>53,685</b>	<b>3,464</b>	<b>57,149</b>

The par value of the Group's issued share capital as at 31 December 2010 was AZN 53,685 thousand (2009: AZN 41,712 thousand).

All ordinary shares have a nominal value of AZN 1,000 per share (2009: AZN 1,000 per share) and rank equally. Each share carries one vote.

As at 31 December 2010, Mr. Etibar Aliyev, the Chairman of the Group's Supervisory Council, owned 15% of the Group's shares (31 December 2009: 15%). As at 31 December 2010, the other major shareholders comprised World Wines 75% (31 December 2009: 75%) and Kazimir Caspian Fund Limited 10% (31 December 2009: 10%). Therefore, the ultimate controlling party of the Group is World Wines. World Wines is a private company registered in the Republic of Azerbaijan, operating in wine production, food processing and agriculture. The company was established on 23 October 2000 and is owned by Mr. Adil Mammadov. Kazimir Caspian Fund Limited ("Kazimir") is a legal entity registered in the Cayman Islands and domiciled in the Russian Federation. Kazimir is an affiliated company to Kazimir Russia Master Fund Limited.

On 10 March 2010, the Group capitalised its retained earnings and issued additional 11,973 ordinary shares with a nominal value of AZN 1,000 per share through a primary registration at the Baku Stock Exchange. The allocation of shares for this transaction was as follows: Mr. Etibar Aliyev – 1,796 shares; Kazimir – 1,198 shares; and World Wines – 8,979 shares. As result of this capitalisation, the Group paid applicable withholding tax of AZN 1,197 thousand on behalf of shareholders and recorded this as a receivable from shareholders. Refer to Note 14.

## 23 Other Reserves

<i>In thousands of Azerbaijani Manats</i>	<b>Available for sale securities</b>	<b>Premises and equipment</b>	<b>Total other reserves</b>
<b>At 1 January 2009</b>	<b>90</b>	<b>2,589</b>	<b>2,679</b>
Revaluation	59	793	852
Realised revaluation reserve	-	(80)	(80)
Income tax effect	-	(159)	(159)
<b>At 31 December 2009</b>	<b>149</b>	<b>3,143</b>	<b>3,292</b>
Revaluation	(31)	-	(31)
Realised revaluation reserve	-	(94)	(94)
<b>At 31 December 2010</b>	<b>118</b>	<b>3,049</b>	<b>3,167</b>

The revaluation reserve for premises is transferred to retained earnings when realised through depreciation, impairment, sale or other disposal.

**Technikabank OJSC**  
**Notes to the Consolidated Financial Statements – 31 December 2010**

**24 Interest Income and Expense**

<i>In thousands of Azerbaijani Manats</i>	<b>2010</b>	<b>2009</b>
<b>Interest income</b>		
Loans and advances to customers	38,752	49,368
Interest income on impaired financial assets	9,790	3,521
Correspondent accounts with other banks	1,016	753
Other investment securities	104	74
<b>Total interest income</b>	<b>49,662</b>	<b>53,716</b>
<b>Interest expense</b>		
Term borrowings from other banks and financial institutions	7,587	12,731
Term deposits of individuals	16,984	10,415
Debt securities in issue	782	3,262
Term deposits of legal entities	1,170	1,110
Other interest expenses	53	9
<b>Total interest expense</b>	<b>26,576</b>	<b>27,527</b>
<b>Net interest income</b>	<b>23,086</b>	<b>26,189</b>

**25 Fee and Commission Income and Expense**

<i>In thousands of Azerbaijani Manats</i>	<b>2010</b>	<b>2009</b>
<b>Fee and commission income</b>		
<i>Fee and commission income in respect of financial instruments not at fair value through profit or loss:</i>		
- Cash transactions	5,384	4,947
- Settlement transactions	2,630	2,696
- Guarantees and letters of credit issued	1,282	1,899
- Plastic cards operations	921	841
- Other	173	121
<b>Total fee and commission income</b>	<b>10,390</b>	<b>10,504</b>
<b>Fee and commission expense</b>		
<i>Fee and commission expense in respect of financial instruments not at fair value through profit or loss:</i>		
- Settlement transactions	410	404
- Guarantees and letters of credit	289	377
- Cash collection	127	273
- Plastic cards operations	1,488	1,062
- Other	208	239
<b>Total fee and commission expense</b>	<b>2,522</b>	<b>2,355</b>
<b>Net fee and commission income</b>	<b>7,868</b>	<b>8,149</b>

## 26 Administrative and Other Operating Expenses

<i>In thousands of Azerbaijani Manats</i>	<i>Note</i>	<b>2010</b>	<b>2009</b>
Staff costs		6,942	6,361
Depreciation of premises and equipment	13	3,790	3,275
Insurance of customer deposit accounts		1,012	481
Rent expenses		719	690
Security services		654	626
Professional services		469	594
Communication		445	395
Taxes other than on income		435	334
Stationery and office supplies		373	339
Repair expenses		370	488
Amortisation of software and other intangible assets	13	261	58
Utilities		152	136
Representative expenses		151	157
Auction expenses		35	-
Advertising and marketing services		33	100
Other		68	299
<b>Total administrative and other operating expenses</b>		<b>15,909</b>	<b>14,333</b>

Included in staff costs are statutory social security costs of AZN 1,122 thousand (2009: AZN 1,060 thousand) and pension contributions of AZN 153 thousand (2009: AZN 144 thousand).

## 27 Income Taxes

Income tax expense comprises the following:

<i>In thousands of Azerbaijani Manats</i>	<b>2010</b>	<b>2009</b>
Current tax charge	1	6
Deferred tax credit	(474)	(550)
<b>Income tax credit for the year</b>	<b>(473)</b>	<b>(544)</b>

The income tax rate applicable to the majority of the Group's income is 20% (2009: 22%). The income tax rate applicable to subsidiaries income is 20% (2009: 22%). On 19 June 2009, the Republic of Azerbaijan reduced the standard corporate income tax rate from 22% to 20% with effect from 1 January 2010.

Reconciliation between the expected and the actual taxation charge is provided below.

<i>In thousands of Azerbaijani Manats</i>	<b>2010</b>	<b>2009</b>
<b>IFRS profit before tax</b>	<b>7,888</b>	<b>8,499</b>
Theoretical tax charge at statutory rate (2010: 20%; 2009: 22%)	(1,577)	(1,870)
Tax effect of items which are not deductible or assessable for taxation purposes:		
- Unrecognised deferred tax	-	(44)
- Non deductible expenses	(164)	(121)
- Effect of changes in income tax rate	-	(55)
Current income tax liability not accrued due to three-year tax holiday	2,214	2,634
<b>Income tax credit/ (expense) for the year</b>	<b>473</b>	<b>544</b>

**27 Income Taxes (continued)**

Differences between IFRS and Azerbaijan statutory taxation regulations give rise to temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and their tax bases. The tax effect of the movements in these temporary differences is detailed below and is recorded at the rate of 20% (2009: 22%).

On 14 November 2008, a new law on “Stimulation of increasing the capitalisation of banks, insurance and reinsurance companies” was enacted in the Republic of Azerbaijan. According to the law the profit tax rate for banks, insurance and reinsurance companies will be applicable at 0% for three fiscal years effective from 1 January 2009, for the portion of the profits transferred to share capital. At 31 December 2010, the management had an intention to take advantage of this concession with regard to the year ended 31 December 2010 and therefore, assessments of the current and deferred taxes were made on this basis.

At 31 December 2010, the tax effects were calculated only for deductible/taxable temporary differences to exist at 1 January 2012, when the tax concession is ineffective. The deferred tax liability recorded in this consolidated financial statement is noncurrent.

<i>In thousands of Azerbaijani Manats</i>	31 December 2009	Charged/ (credited) to profit or loss	31 December 2010
<b>Tax effect of deductible/(taxable) temporary differences</b>			
Gains arising from a change in fair value of investment property	512	-	512
Premises and equipment	549	423	972
Provision on credit related commitments	-	-	-
Provision on loans to banks	(90)	(892)	(982)
Provision on investment	-	47	47
Reversed insurance reserves	-	40	40
Reposessed asset impairment	-	(92)	(92)
<b>Deferred tax (asset)/liability</b>	<b>971</b>	<b>(474)</b>	<b>497</b>

In the context of the Group's current structure and Azerbaijani tax legislation, tax losses and current tax assets of different group companies may not be offset against current tax liabilities and taxable profits of other group companies and, accordingly, taxes may accrue even where there is a consolidated tax loss.

Therefore, deferred tax assets and liabilities are offset only when they relate to the same taxable entity.

<i>In thousands of Azerbaijani Manats</i>	31 December 2008	Charged/ (credited) to profit or loss	Charged directly to equity	31 December 2009
<b>Tax effect of deductible/(taxable) temporary differences</b>				
Gains arising from a change in fair value of investment property	490	22	-	512
Premises and equipment	873	(483)	159	549
Provision on loans to banks	-	(90)	-	(90)
<b>Deferred tax liability</b>	<b>1,363</b>	<b>(551)</b>	<b>159</b>	<b>971</b>

**28 Earnings per Share**

Basic earnings per share are calculated by dividing the profit or loss attributable to equity holders of the Bank by the weighted average number of ordinary shares in issue during the year.

The Group has no dilutive potential ordinary shares; therefore, the diluted earnings per share equal the basic earnings per share.

<i>In thousands of Azerbaijani Manats except for number of shares</i>	<b>2010</b>	<b>2009</b>
Profit for the year attributable to ordinary shareholders	8,361	9,043
<b>Profit for the year</b>	<b>8,361</b>	<b>9,043</b>
Weighted average number of ordinary shares in issue	53,685	53,685
<b>Basic earnings per ordinary share</b>	<b>0.156</b>	<b>0.168</b>

The weighted average number of shares for the financial year ended 31 December 2009 was adjusted as a result of capitalisation of profits which occurred during 2010, as per requirement of IAS 33 "Earnings per share."

**29 Segment Analysis**

Starting from 1 January 2009, the Group prepares its segment analysis in accordance with IFRS 8, *Operating segments*, which replaced IAS 14, *Segment reporting*.

Following the management approach of IFRS 8, operating segments are reported in accordance with the internal reporting provided to the Board of Directors (the chief operating decision-maker), which is responsible for allocating resources to the reportable segments and assesses its performance. All operating segments used by the Group meet the definition of a reportable segment under IFRS 8.

**Business Segments.** The Group is organised on a basis of two main business segments:

- Retail banking – representing private banking services, private customer current accounts, savings, deposits, investment savings products, custody, credit and debit cards, consumer loans and mortgages.
- Corporate banking – representing direct debit facilities, current accounts, deposits, overdrafts, loan and other credit facilities, foreign currency and derivative products.

There are no other material items of income or expense between the business segments. Segment assets and liabilities comprise operating assets and liabilities, being the majority of the balance sheet, but excluding taxation.

The Board of Directors reviews financial information prepared based on Azerbaijan accounting standards adjusted to meet the requirements of internal reporting. Such financial information differs in certain aspects from International Financial Reporting Standards:

- (i) funds are generally reallocated between segments at internal interest rates set by the treasury department, which are determined by reference to market interest rate benchmarks, contractual maturities for loans and observed actual maturities of customer accounts balances;
- (ii) income taxes are not allocated to segments;
- (iii) loan provisions are recognized based on management judgment and availability of information rather than based on the incurred loss model prescribed in IAS 39; and

## 29 Segment Analysis (Continued)

Segment information for the main reportable business segments of the Group for the years ended 31 December 2010 and 2009 is set out below:

<i>In thousands of Azerbaijani Manats</i>	Retail banking		Corporate banking		Total	
	2010	2009	2010	2009	2010	2009
<b>Total segment revenues</b>	<b>21,459</b>	<b>16,226</b>	<b>40,714</b>	<b>50,574</b>	<b>62,173</b>	<b>66,800</b>
<b>Total revenues comprise:</b>						
- Interest income	16,264	12,979	33,398	40,737	49,662	53,716
- Fee and commission income	3,423	2,419	6,967	8,085	10,390	10,504
- Gains less losses from trading in foreign currencies	615	197	1,252	657	1,867	854
- Gains arising from a change in fair value of investment property	-	49	-	62	-	111
- Foreign exchange translation losses less gains	542	161	1,076	487	1,618	648
Reversal of provision/(provision charge for) of due from other banks	-	-	1,628	-	1,628	-
- Insurance premiums written	1,203	412	1,025	514	2,228	926
- Other operating income	20	9	40	32	60	41
<b>Total segment revenues</b>	<b>22,067</b>	<b>16,226</b>	<b>45,386</b>	<b>50,574</b>	<b>67,453</b>	<b>66,800</b>
Interest expense	(8,914)	(6,670)	(17,662)	(20,857)	(26,576)	(27,527)
Provision for loan impairment	(2,922)	(2,945)	(5,799)	(8,870)	(8,721)	(11,815)
Provision for impairment of due from other banks	-	(557)	-	(692)	-	(1,249)
Fee and commission expense	(831)	(542)	(1,691)	(1,813)	(2,522)	(2,355)
Loss on revaluation of premises	-	(1,061)	-	(1,327)	-	(2,388)
Reinsurance premiums ceded	(170)	(39)	(144)	(48)	(314)	(87)
Decrease/(Increase) of provision for unearned premiums	17	64	35	214	52	278
Increase of reinsurer's share of provision for unearned premium	(93)	(20)	(189)	(69)	(282)	(89)
Net claims incurred	(97)	(60)	(197)	(202)	(294)	(262)
Provision for losses on credit related commitments	(62)	(78)	(53)	(98)	(115)	(176)
Administrative and other operating expenses	(5,370)	(3,515)	(10,539)	(10,818)	(15,909)	(14,333)
<b>Adjusted profit/(loss) before income tax</b>	<b>3,625</b>	<b>803</b>	<b>9,147</b>	<b>5,994</b>	<b>12,772</b>	<b>6,797</b>
<i>In thousands of Azerbaijani Manats</i>						
	2010		2009			
<b>Adjusted profit before income tax for reportable segments</b>	<b>12,772</b>		<b>6,797</b>			
<i>Non Allocated:</i>						
- Impairment of repossessed assets	(477)				-	
<i>Adjustments to bring management information in line with IFRS:</i>						
- Increase of statutory charge for loan impairment	(3,969)				2,231	
- Reversal of statutory charge for impairment of due from other banks	(438)				(529)	
<b>Profit before income tax</b>	<b>7,888</b>				<b>8,499</b>	



## 29 Segment Analysis (Continued)

<i>In thousands of Azerbaijani Manats</i>	Retail Banking		Corporate banking			Total
	31 December 2010	31 December 2009	31 December 2010	31 December 2009	31 December 2010	31 December 2009
<b>Total segment assets</b>	<b>194,588</b>	<b>132,568</b>	<b>303,147</b>	<b>315,936</b>	<b>497,735</b>	<b>448,504</b>
Deferred income tax asset	-	-	-	-	-	-
<b>Total assets</b>	<b>194,588</b>	<b>132,568</b>	<b>303,133</b>	<b>315,936</b>	<b>497,735</b>	<b>448,504</b>
<b>Total segment liabilities</b>	<b>236,217</b>	<b>162,726</b>	<b>186,089</b>	<b>227,914</b>	<b>422,306</b>	<b>448,504</b>
Current income tax liability						-
Deferred income tax liability					497	971
<b>Total liabilities</b>	<b>236,217</b>	<b>162,726</b>	<b>186,089</b>	<b>227,914</b>	<b>422,803</b>	<b>391,611</b>
<i>In thousands of Azerbaijani Manats</i>					<b>2010</b>	<b>2009</b>
Total segment assets					<b>497,735</b>	<b>453,807</b>
Adjustments to bring management information in line with IFRS:						
- Increase of statutory charge for loan impairment					(8,098)	(4,130)
- Reversal of statutory charge for impairment of due from other banks					91	529
<b>Total assets per statement of financial position</b>					<b>489,728</b>	<b>444,903</b>

### **Geographical segments.**

As at 31 December 2010 and 31 December 2009 all non-current assets are located in Azerbaijan .

## 30 Financial Risk Management

The risk management function within the Group is carried out in respect of financial risks (credit, market, geographical, currency, liquidity and interest rate), operational risks and legal risks. The primary objectives of the financial risk management function are to establish risk limits, and then ensure that exposure to risks stays within these limits. The operational and legal risk management functions are intended to ensure proper functioning of internal policies and procedures to minimise operational and legal risks.

**Credit risk.** The Group takes on exposure to credit risk, which is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. Exposure to credit risk arises as a result of the Group's lending and other transactions with counterparties giving rise to financial assets.

### 30 Financial Risk Management (Continued)

Management of credit risk is an integral part of the Group's operations. Risk management covers all stages of the credit process, from loan origination and credit approval to collection. The Bank's Risk Management, Asset Liability Committee ("ALCO"), and Credit Committees meet regularly and report at least once a month to the Supervisory Board. The committees have clearly defined responsibilities and guidelines for maximum risk levels in accordance with the CBAR's Risk Management Standards and Procedures, approved by the Management Board of the CBAR as of 29 December 2004, classification of assets and the Bank's internal asset management policy. Under the CBAR Risk Management Standards and Procedures established by the CBAR, the process of risk management entails the control over and reduction of risks through their determination and evaluation, the preparation of reports about such risks (for example, by the Executive Board, the committees and the risk management officers) and the adoption by the Supervisory Board of risk limits.

These are the primary objectives of the risk management function which are described below. Under the CBAR Risk Management Standards, the risk management infrastructure and the risks of a bank must be evaluated by an outside specialist or auditor at least once a year. Generally, the CBAR's standards require the Bank to adopt an appropriate methodology to evaluate risks, though no specific quantitative limits or standards are prescribed.

The risk management function is within the overall structure of the duties and powers of all bank personnel, from the supervisory board down to the employees of a bank. This function requires the determination of: (i) the volume or levels of the risks controlled by the risk management function, (ii) the position of the body responsible for the performance of risk management functions within the internal organisational structure of the bank and (iii) the methodology used to evaluate information about the risks, prepare reports thereon, control such risks (i.e., determine their limits) and taking such information into account as part of the decision-making process. The structure of the risk management function consists of the risk management responsibilities borne by each of the Supervisory Board, Executive Board and the Risk Management, ALCO and Credit Committees as well as the risk management divisions or departments within a bank. The Bank's internal asset management policy is the same as required by the standards set by the CBAR.

The CBAR Risk Management Standards explain the nature of credit risks as well as their measurement and evaluation methodology. Furthermore, the Standards envision the adoption by the supervisory board of a bank of the following risk limits: limits for capital exposed to risk, market risk limits, credit risk limits as well as concentration risk limits.

The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored on a day-to-day basis by the relevant responsible sections of the Bank such as the Credit Committee. Such risks are also monitored on a monthly basis by the Risk Management Committee and are subject to an annual or more frequent review of risk management procedures by the Risk Management Committee for possible overhaul to improve procedures, if the need arises to reduce the number of overdue loans. Limits on the level of credit risk by product, borrower and industry sector are reviewed regularly by the Executive Board.

The exposure to any one borrower, including banks and brokers, is further restricted by the CBAR regulatory sub-limits covering on and off-balance sheet exposures and daily delivery risk limits in relation to trading items such as forward foreign exchange contracts. Actual exposures against limits are monitored daily. The following sub-limits are applied by the Group:

(1) the maximum loan amount for one borrower or related borrowers' group is, as follows:

- (i) 20 per cent of the Bank's total equity if the market value of the collateral is at least equal to 150 per cent of the value of the loan; and
- (ii) 7 per cent of the Bank's total equity if the market value of the collateral is less than 150 per cent of the value of the loan;

### 30 Financial Risk Management (Continued)

(2) for large loans without collateral exceeding 10 per cent of the Bank's total equity, such loans in aggregate must not exceed 800 per cent in total of the Bank's total equity;

(3) the total maximum amount of the Bank's loans to related parties must not exceed

- (i) 20 per cent of the Bank's total equity; and
- (ii) 10 per cent of the Bank's equity per legal person; or
- (iii) 3 per cent of the Bank's equity per physical person.

Exposure to credit risk is managed through the regular analysis of the ability of borrowers and potential borrowers to meet interest and principal repayment obligations and by changing these lending limits where appropriate. This analysis is undertaken on a monthly basis by the Credit Committee. The analysis is based on information including overdue payments due to the Group, any changes in the financial condition of the Group's customers, substantial changes in any segment of the market or country's economic sector, or any negative information regarding the customer's reputation. The analysis also takes into consideration the Group's consolidated exposure to credit risk at the time the analysis is performed. This allows the Group to assess whether any preventive measures are needed to avoid these risks.

The Group's consolidated maximum exposure to credit risk is primarily reflected in the carrying amounts of financial assets on the consolidated balance sheet. The impact of possible netting of assets and liabilities to reduce potential credit exposure is not significant. For guarantees and commitments to extend credit, the maximum exposure to credit risk is the amount of the commitment. Refer to Note 33.

Credit risk for off-balance sheet financial instruments is defined as the possibility of sustaining a loss as a result of another party to a financial instrument failing to perform in accordance with the terms of the contract. The Group uses the same credit policies in making conditional obligations as it does for on-balance sheet financial instruments through established credit approvals, risk control limits and monitoring procedures.

The Group's credit department reviews ageing analysis of outstanding loans and follows up past due balances. Management, therefore, considers it appropriate to provide ageing and other information about credit risk as disclosed in 8, 9, 10 and 14.

**Credit approval process and structure.** Management believes the credit approval process described below enhances its ability to accurately monitor and limit its credit exposure. Under the Bank's credit approval structure, smaller loans (loans up to AZN 5 thousand) may be issued by local branches while larger loans are issued by the head office. The Bank has established the following credit approval structures:

(1) Each of the Bank's branches has a credit officer. Each branch credit officer is authorised to approve loans of up to AZN 5 thousand. Although the branches do not have any aggregate lending limits, they are monitored regularly by the Bank's head office for any unusual lending activities.

(2) The Credit Committee at the head office in Baku is authorised to extend loans of up to AZN 100 thousand.

(3) All loans exceeding AZN 100 thousand but less than AZN 300 thousand must also be approved by the Executive Board in addition to the Credit Committee. Loans over AZN 300 thousand and all transactions with related parties must be approved by the Supervisory Board in accordance with Article 25 of the Azerbaijani Law on Banks. The Bank intends to implement an internal policy in 2010 whereby no more than 20 per cent of its loan portfolio is comprised of loans in each sector in which its clients operate.

(4) The pricing of the loan is based on a number of factors including the inflation rate, average cost of funding and the premium imposed by the Bank for the specific loan type and the customer risk profile.



**30 Financial Risk Management (Continued)**

**Market risk.** The Group takes on exposure to market risks. Market risks arise from open positions in (a) currency, (b) interest rate and (c) equity products, all of which are exposed to general and specific market movements. The goal of the Group's market risk management is to limit and reduce the amount of possible losses on open market positions that may be incurred by the Bank due to negative changes in currency exchange rates and interest rates. The Executive Board sets limits on the value of risk that may be accepted, which is monitored on a daily basis. These limits are set in accordance with the CBAR guidelines on *Determining and Regulating the Open Foreign Currency Position*. The open currency position of the Bank in any single currency may not exceed 10.0 per cent, and in all foreign currencies 20.0 per cent of the Bank's total equity. The Bank's management uses its discretion to apply limits stricter than those of CBAR if it believes such action is necessary.

**Currency risk.** The Bank takes on exposure to effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Executive Board sets limits on the level of exposure by currency and in total for both overnight and intra-day positions, which are monitored daily. The Bank does not deal in any derivative instruments for speculative or hedging purposes. Such instruments are not commonly used in Azerbaijan.

In accordance with the guidelines of the management board of the CBAR on *Determining and Regulating the Open Foreign Currency Position*, the open foreign currency position of the Bank in any single currency should not exceed 10 per cent, and in all foreign currencies, 20 per cent of the Bank's total equity.

The Bank has exposure to the US Dollar. The Bank expects the Azerbaijani Manat to appreciate against the US Dollar in the future, therefore the Bank's policy has been to make loans mostly in Azerbaijani Manats. Management believes that the Bank will be able to obtain the resources necessary in order to cover any losses resulting from open currency positions without a material impact on the Bank, and is actively taking measures to reduce such risks. These measures include active forecasting the appreciation of the Azerbaijani Manat against the US Dollar, as well as monitoring studies by the International Monetary Fund.

The table below summarises the Group's consolidated exposure to foreign currency exchange rate risk at the end of the reporting date:

<i>In thousands of Azerbaijani Manats</i>	2010			2009		
	Monetary financial assets	Monetary financial liabilities	Net position	Monetary financial assets	Monetary financial liabilities	Net position
Azerbaijani Manats	378,175	306,124	72,051	344,022	283,491	60,531
US Dollars	36,607	87,445	(50,838)	51,819	81,082	(29,263)
Euro	4,441	25,353	(20,912)	7,737	22,114	(14,377)
Other	707	1,270	(563)	850	1,604	(754)
<b>Total</b>	<b>419,930</b>	<b>420,192</b>	<b>(262)</b>	<b>404,428</b>	<b>388,291</b>	<b>16,137</b>

The above analysis includes only monetary assets and liabilities. Investments in equities and non-monetary assets are not considered to give rise to any material currency risk.

During the years ended 31 December 2010 and 31 December 2009, the Bank has entered into forward foreign exchange contracts. Although the Management believes that those contracts do not meet the definition of financial derivatives, (because their underlining fair values are equal to zero) they are considered as forward foreign exchange agreement as per CBAR regulations and are effective in reducing the Bank's open foreign currency exposure. Consequently, the Management included these instruments in calculation of open foreign currency limits as an integral part of the Bank's foreign currency position, and believes that the Bank is fully compliant with the covenants related to the open currency position as at 31 December 2010, except for the breach outlined in Note 33.

### 30 Financial Risk Management (Continued)

The following table presents sensitivities of profit and loss and equity to reasonably possible changes in exchange rates applied at reporting date, with all other variables held constant:

<i>In thousands of Azerbaijani Manats</i>	2010	2009
	Impact on profit or loss and equity	Impact on profit or loss and equity
US Dollars strengthening by 5%	(2,540)	(1,463)
US Dollars weakening by 5%	2,540	1,463
Euro strengthening by 15%	(1,046)	(2,157)
Euro weakening by 15%	1,046	2,157
Other strengthening by 5%	(28)	(38)
Other weakening by 5%	28	38

Other than as a result of any impact on the Group's consolidated profit or loss, there is no other impact on the Group's consolidated equity as a result of such changes in exchange rates. The exposure was calculated only for monetary balances denominated in currencies other than the functional currency of the respective entity of the Group.

The Group's exposure to currency risk at reporting date is not representative of the typical exposure during the year. The following table presents sensitivities of profit and loss and equity to reasonably possible changes in exchange rates applied to average exposure to currency risk during the year, with all other variables held constant:

<i>In thousands of Azerbaijani Manats</i>	Average exposure during 2010	Average exposure during 2009
	Impact on profit or loss and equity	Impact on profit or loss and equity
US Dollars strengthening by 5%	(2,523)	(1,871)
US Dollars weakening by 5%	2,523	1,871
Euro strengthening by 5%	(1,898)	(2,499)
Euro weakening by 5%	1,898	2,499
RUR strengthening by 5%	15	3
RUR weakening by 5%	(15)	(3)
GBP strengthening by 5%	(56)	(40)
GBP weakening by 5%	56	40

Other than as a result of any impact on the Group's consolidated profit or loss, there is no other impact on the Group's consolidated equity as a result of such changes in exchange rates.

**Interest rate risk.** The table below summarises the Group's consolidated exposure to interest rate risks. The table presents the aggregated amounts of the Group's consolidated financial assets and liabilities at carrying amounts, categorised by the earlier of contractual interest re-pricing or maturity dates.

<i>In thousands of Azerbaijani Manats</i>	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	More than 1 year	Over 5 years	Total
<b>31 December 2010</b>						
Total financial assets	100,500	38,828	102,857	116,588	64,952	423,725
Total financial liabilities	123,116	33,837	133,542	62,431	67,266	420,192
<b>Net interest sensitivity gap at 31 December 2010</b>	<b>(22,616)</b>	<b>4,991</b>	<b>(30,685)</b>	<b>54,157</b>	<b>(2,314)</b>	<b>3,533</b>
<b>31 December 2009</b>						
Total financial assets	83,832	20,264	202,360	73,225	24,747	404,428
Total financial liabilities	111,889	16,917	199,096	23,239	37,150	388,291
<b>Net interest sensitivity gap at 31 December 2009</b>	<b>(28,057)</b>	<b>3,347</b>	<b>3,264</b>	<b>49,986</b>	<b>(12,403)</b>	<b>16,137</b>

**30 Financial Risk Management (Continued)**

The Group's profit is not exposed to market interest rate changes because the Group does not have variable interest assets or liabilities. In addition to that, in the recent years average interest rates on financial instruments has not shown significant volatility in Azerbaijani banking market.

The Group monitors effective interest rates for its financial instruments.

The table below summarises interest rates based on reports reviewed by key management personnel:

<i>In % p.a.</i>	2010				2009			
	AZN	USD	Euro	Other	AZN	USD	Euro	Other
<b>Assets</b>								
Cash and cash equivalents	-	-	-	-	-	-	-	-
Due from other banks	12	11	-	-	15	18	-	-
Loans and advances to customers	15	16	18	-	15	16	18	-
Other Investment securities	3	-	-	-	3	-	-	-
<b>Liabilities</b>								
Due to other banks	10	10	5	-	12	8	13	-
Customer accounts	-	-	-	-	-	-	-	-
- current and settlement accounts	-	5	-	-	-	-	-	-
- term deposits	10	11	11	12	12	14	12	13
Debt securities in issue	14	15	-	-	14	14	-	-
Term borrowings from other banks and financial institutions	6	3	1	-	2	6	-	-

### 30 Financial Risk Management (Continued)

**Geographical risk concentrations.** The geographical concentration of the Group's consolidated financial assets and liabilities at 31 December 2010 is set out below.

Assets, liabilities and credit related commitments have been based on the country, in which the counterparty is located. Cash on hand, investment property and premises and equipment have been allocated based on the country, in which they are physically held.

<i>In thousands of Azerbaijani Manats</i>	<b>Azerbaijan</b>	<b>OECD</b>	<b>Non-OECD</b>	<b>Total</b>
<b>Assets</b>				
Cash and cash equivalents	43,861	814	567	45,242
Mandatory cash balances with the CBAR	1,102	-	-	1,102
Due from other banks and financial institutions	5,947	-	-	5,947
Loans and advances to customers	353,447	-	-	353,447
Investment securities available for sale	460	393	-	853
Other investment securities	12,312	667	-	12,979
Other financial assets	1,692	1,955	508	4,155
<b>Total financial assets</b>	<b>418,821</b>	<b>3,829</b>	<b>1,075</b>	<b>423,725</b>
<b>Non-financial assets</b>	<b>66,003</b>	<b>-</b>	<b>-</b>	<b>66,003</b>
<b>Total assets</b>	<b>484,824</b>	<b>3,829</b>	<b>1,075</b>	<b>489,728</b>
<b>Liabilities</b>				
Due to other banks and financial institutions	19,669	-	-	19,669
Customer accounts	271,386	-	-	271,386
Debt securities in issue	914	-	2,423	3,337
Term borrowings from other banks and other financial institutions	119,254	5,944	-	125,198
Other financial liabilities	492	6	104	602
<b>Total financial liabilities</b>	<b>411,715</b>	<b>5,950</b>	<b>2,527</b>	<b>420,192</b>
<b>Non-financial liabilities</b>	<b>2,611</b>	<b>-</b>	<b>-</b>	<b>2,611</b>
<b>Total liabilities</b>	<b>414,326</b>	<b>5,950</b>	<b>2,527</b>	<b>422,803</b>
<b>Net on balance sheet position of financial instruments</b>	<b>70,498</b>	<b>(2,121)</b>	<b>(1,452)</b>	<b>66,925</b>
<b>Credit related commitments (Note 33)</b>	<b>14,569</b>	<b>-</b>	<b>-</b>	<b>14,569</b>

**30 Financial Risk Management (Continued)**

The geographical concentration of the Group's consolidated assets and liabilities at 31 December 2009 is set out below:

<i>In thousands of Azerbaijani Manats</i>	<b>Azerbaijan</b>	<b>OECD</b>	<b>Non-OECD</b>	<b>Total</b>
<b>Assets</b>				
Cash and cash equivalents	45,845	1,091	961	47,897
Mandatory cash balances with the CBAR	837	-	-	837
Due from other banks and financial institutions	6,979	1	-	6,980
Loans and advances to customers	342,509	-	-	342,509
Investments	460	149	-	609
Investment securities available for sale	2,336	-	-	2,336
Other financial assets	715	1,835	710	3,260
<b>Total financial assets</b>	<b>399,681</b>	<b>3,076</b>	<b>1,671</b>	<b>404,428</b>
<b>Non-financial assets</b>	<b>45,778</b>	<b>-</b>	<b>-</b>	<b>45,778</b>
<b>Total assets</b>	<b>445,459</b>	<b>3,076</b>	<b>1,671</b>	<b>450,206</b>
<b>Liabilities</b>				
Due to other banks and financial institutions	28,826	-	-	28,826
Customer accounts	189,812	-	-	189,812
Debt securities in issue	2,921	-	7,985	10,906
Term borrowings from other banks and other financial institutions	152,190	4,817	-	157,007
Other financial liabilities	1,232	-	508	1,740
<b>Total financial liabilities</b>	<b>374,981</b>	<b>4,817</b>	<b>8,493</b>	<b>388,291</b>
<b>Non-financial liabilities</b>	<b>3,320</b>	<b>-</b>	<b>-</b>	<b>3,320</b>
<b>Total liabilities</b>	<b>378,301</b>	<b>4,817</b>	<b>8,493</b>	<b>391,611</b>
<b>Net on-balance sheet position of financial instruments</b>	<b>67,158</b>	<b>(1,741)</b>	<b>(6,822)</b>	<b>58,595</b>
<b>Credit related commitments (Note 33)</b>	<b>8,819</b>	<b>-</b>	<b>-</b>	<b>8,819</b>



**30 Financial Risk Management (Continued)**

**Liquidity risk.** Liquidity risk is defined as the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities. The Group is exposed to daily calls on its available cash resources from overnight deposits, current accounts, maturing deposits, loan draw downs, and guarantees. The Group does not maintain cash resources to meet all of these needs as experience shows that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty. Liquidity risk is managed by the Asset/Liability Committee of the Group.

The Group seeks to maintain a stable funding base comprising primarily amounts due to other banks, corporate and retail customer deposits and debt securities and invest the funds in diversified portfolios of liquid assets, in order to be able to respond quickly and smoothly to unforeseen liquidity requirements.

The liquidity management of the Group requires considering the level of liquid assets necessary to settle obligations as they fall due; maintaining access to a range of funding sources; maintaining funding contingency plans and monitoring balance sheet liquidity ratios against regulatory requirements.

The Group calculates liquidity ratios on a monthly basis in accordance with the requirement of the CBAR. According to instructions set by the Central Bank of Azerbaijan, the Bank calculates instant liquidity as a ratio of daily average liquid assets to daily average liquid liabilities. The ratio was 46.55% at 31 December 2010 (2009: 67%). These ratios are calculated based on balances derived from statutory financial statements as at 31 December 2010.

The Treasury Department receives information about the liquidity profile of the consolidated financial assets and liabilities. The Treasury then provides for an adequate portfolio of short-term liquid assets, largely made up of short-term liquid trading securities, deposits with banks and other inter-bank facilities, to ensure that sufficient liquidity is maintained within the Group as a whole.

The table below shows liabilities at 31 December 2010 by their remaining contractual maturity. The amounts disclosed in the maturity table are the contractual undiscounted cash flows. Such undiscounted cash flows differ from the amount included in the consolidated statement of financial position because the statement of financial position amount is based on discounted cash flows.

When the amount payable is not fixed, the amount disclosed is determined by reference to the conditions existing at the end of the reporting date. Foreign currency payments are translated into AZN using official exchange rate of AZN to foreign currencies established by the CBAR at the end of the reporting date.

The undiscounted maturity analysis of financial assets and liabilities at 31 December 2010 is as follows:

	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 12 months to 5 years	Over 5 years	Total
<i>In thousands of Azerbaijani Manats</i>						
<b>Liabilities</b>						
Due to other banks and financial institutions	5,034	130	10,094	4,787	-	20,045
Customer accounts – individuals	89,032	3,139	16,528	141,112	3,345	253,156
Customer accounts – other	7,043	229	9,498	12,416	-	29,186
Debt securities in issue	140	213	241	3,341	-	3,935
Term borrowings from other banks and financial institutions	5,174	3,545	6,281	53,905	81,705	150,610
Other financial liabilities	394	-	208	-	-	602
Import letters of credit (Note 33)	3,832	-	-	-	-	3,832
Guarantees issued (Note 33)	8,539	-	-	-	-	8,539
Undrawn credit lines (Note 33)	2,198	-	-	-	-	2,198
<b>Total potential future payments for financial obligations</b>	<b>121,386</b>	<b>7,256</b>	<b>42,850</b>	<b>215,561</b>	<b>85,050</b>	<b>472,103</b>

### 30 Financial Risk Management (Continued)

The undiscounted maturity analysis of financial liabilities at 31 December 2009 is as follows:

<i>In thousands of Azerbaijani Manats</i>	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 12 months to 5 years	Over 5 years	Total
<b>Liabilities</b>						
Due to other banks and financial institutions	9,118	455	20,754	-	-	30,327
Customer accounts – individuals	26,288	7,197	80,069	10,223	299	124,076
Customer accounts – other	66,806	4,156	4,088	-	-	75,050
Debt securities in issue	265	7,874	400	4,605	-	13,144
Term borrowings from other banks and financial institutions	11,563	486	95,801	12,633	45,190	165,673
Other financial liabilities	766	125	849	-	-	1,740
Import letters of credit (Note 33)	7,303	-	-	-	-	7,303
Guarantees issued (Note 33)	1,402	-	-	-	-	1,402
Undrawn credit lines (Note 33)	290	-	-	-	-	290
<b>Total potential future payments for financial obligations</b>	<b>123,801</b>	<b>20,293</b>	<b>201,961</b>	<b>27,461</b>	<b>45,489</b>	<b>419,005</b>

Customer accounts are classified in the above analysis based on contractual maturities. However, in accordance with Azerbaijan Civil Code, individuals have a right to withdraw their deposits prior to maturity if they forfeit their right to accrued interest.

The Group does not use the above undiscounted maturity analysis to manage liquidity. Instead, the Group monitors expected maturities, which may be summarised, as follows at 31 December 2010:

<i>In thousands of Azerbaijani Manats</i>	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 12 months to 5 years	Over 5 years	Total
<b>Assets</b>						
Cash and cash equivalents	45,242	-	-	-	-	45,242
Mandatory cash balances with CBAR	1,102	-	-	-	-	1,102
Due from other banks and financial institutions	955	130	3,164	1,698	-	5,947
Loans and advances to customers	52,362	38,576	84,868	114,313	63,328	353,447
Investments	-	-	276	577	-	853
Other investment securities	-	-	12,979	-	-	12,979
Other financial assets	839	122	1,570	-	1,624	4,155
<b>Total financial assets</b>	<b>100,500</b>	<b>38,828</b>	<b>102,857</b>	<b>116,588</b>	<b>64,952</b>	<b>423,725</b>
<b>Liabilities</b>						
Due to other banks and financial institutions	4,920	-	9,962	4,787	-	19,669
Customer accounts	112,855	31,062	114,464	12,949	56	271,386
Debt securities in issue	-	140	-	3,197	-	3,337
Term borrowings from other banks and financial institutions	4,947	2,635	4,091	41,498	72,027	
Other financial liabilities	394	-	208	-	-	602
<b>Total financial liabilities</b>	<b>123,116</b>	<b>33,837</b>	<b>128,725</b>	<b>62,431</b>	<b>72,083</b>	<b>420,192</b>
<b>Net liquidity gap at 31 December 2010</b>	<b>(22,616)</b>	<b>4,991</b>	<b>(25,868)</b>	<b>54,157</b>	<b>(7,131)</b>	<b>3,533</b>
<b>Cumulative liquidity gap at 31 December 2010</b>	<b>(22,616)</b>	<b>(17,625)</b>	<b>(43,493)</b>	<b>10,664</b>	<b>3,533</b>	

### 30 Financial Risk Management (Continued)

The analysis by expected maturities may be summarised, as follows at 31 December 2009:

	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 12 month s to 5 years	Over 5 years	Total
<i>In thousands of Azerbaijani Manats</i>						
<b>Assets</b>						
Cash and cash equivalents	47,897	-	-	-	-	47,897
Mandatory cash balances with CBAR	66	74	623	74	-	837
Due from other banks and financial institutions	320	93	3,179	3,388	-	6,980
Loans and advances to customers	34,493	20,097	196,354	69,004	22,561	342,509
Investment securities available for sale	-	-	-	609	-	609
	-	-	-	150	2,186	2,336
Other financial assets	1,056	-	2,204	-	-	3,260
<b>Total financial assets</b>	<b>83,832</b>	<b>20,264</b>	<b>202,360</b>	<b>73,225</b>	<b>24,747</b>	<b>404,428</b>
<b>Liabilities</b>						
Due to other banks and financial institutions	8,874	-	19,952	-	-	28,826
Customer accounts	92,008	9,356	78,983	9,326	139	189,812
Debt securities in issue	265	7,436	-	3,205	-	10,906
Term borrowings from other banks and other financial institutions	9,976	-	94,495	10,708	41,828	157,007
Other financial liabilities	766	125	849	-	-	1,740
<b>Total financial liabilities</b>	<b>111,889</b>	<b>16,917</b>	<b>194,279</b>	<b>23,239</b>	<b>41,967</b>	<b>388,291</b>
<b>Net liquidity gap at 31 December 2009</b>	<b>(28,057)</b>	<b>3,347</b>	<b>8,081</b>	<b>49,986</b>	<b>(17,220)</b>	<b>16,137</b>
<b>Cumulative liquidity gap at 31 December 2009</b>	<b>(28,057)</b>	<b>(24,710)</b>	<b>(16,629)</b>	<b>33,357</b>	<b>16,137</b>	

The matching and/or controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Group. It is unusual for banks ever to be completely matched since business transacted is often of an uncertain term and of different types. An unmatched position potentially enhances profitability, but can also increase the risk of losses. The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature, are important factors in assessing the liquidity of the Group and its consolidated exposure to changes in interest and exchange rates.

Management believe that despite a substantial portion of customers accounts being on demand, diversification of these deposits by number and type of depositors, and the past experience of the Group would indicate that these customers' accounts provide a long-term and stable source of funding for the Group.

Liquidity requirements to support calls under guarantees and standby letters of credit are considerably less than the amount of the commitment because the Group does not generally expect the third party to draw funds under the agreement. The total outstanding contractual amount of commitments to extend credit does not necessarily represent future cash requirements, since many of these commitments will expire or terminate without being funded.

### 31 Management of Insurance Risk

**Insurance risk.** The risk under any one insurance contract is the possibility that the insured event occurs and the uncertainty of the amount of the resulting claim. By the very nature of an insurance contract, this risk is random and therefore unpredictable for each individual insurance contract.

For a portfolio of insurance contracts where the theory of probability is applied to pricing and provisioning, the principal risk that the Group faces under its insurance contracts is that the actual claims and benefit payments exceed the carrying amount of the insurance liabilities. This could occur because the frequency or severity of claims and benefits are greater than estimated. Insured events are random and the actual number and amount of claims and benefits will vary from year to year from the level established using statistical techniques.

The Group manages its insurance risk by means of established internal procedures which include underwriting authority levels, pricing policy, approved reinsurers list and ongoing monitoring.

**Estimation of insurance loss reserves.** Loss provisions are calculated based on the Group's historical data. In calculating the estimated cost of unpaid claims (both reported and not), the Group's estimation techniques include a combination of loss ratio-based estimates (where the loss ratio is defined as the ratio between the ultimate cost of insurance claims and insurance premiums earned in a particular financial year in relation to such claims) and an estimate based upon actual claims experience using predetermined formulae where a greater weight is given to actual claims experience as time passes.

The initial loss ratio estimate is an important assumption in the estimation technique and is based on previous years' experience, adjusted for factors such as premium rate changes, anticipated market experience and historical claims inflation. The initial estimate of the loss ratios used for the current year (before reinsurance) are analysed by type of risk for current and prior year premiums earned.

**Sources of uncertainty in the estimation of future claim payments.** Claims on insurance contracts are payable on a claims-occurrence basis. The Group is liable for all insured events that occurred during the term of the contract, if the loss is discovered before the end of the contract term. As a result, liability claims are settled within a short period of time, which historically has not exceeded 3 months from the end of the contract term. There are several variables that affect the amount and timing of cash flows from insurance contracts. These mainly relate to the inherent risks of the activities carried out by both corporate and individual contract holders and the risk management procedures they adopted. The compensation paid on insurance contracts in the Group's portfolio primarily consists of monetary awards granted for:

- medical insurance;
- physical damage to motor vehicles (for motor vehicle insurance covers);
- financial loss, bodily injury and physical damage suffered by the third parties (caused by the vehicle owners); and
- physical damage to property (for property insurance covers).

Such awards are lump-sum payments that are calculated by the Group's in-house underwriters as the present value of the lost earnings and rehabilitation expenses that the injured party will incur as a result of the accident.

**Reinsurance policy.** An element of the Group's motor, property, third party liability, employer liability and cargo portfolios is reinsured with local and foreign insurance companies under reinsurance agreements that reduce the potential maximum exposure that the Group is subject to.

**Diversification.** Experience shows that the larger the portfolio of similar insurance contracts, the smaller the relative variability about the expected outcome will be. In addition, a more diversified portfolio is less likely to be affected by a change in any subset of the portfolio. The Group has developed its insurance underwriting strategy to diversify the type of insurance risks accepted and within each of these categories to achieve a sufficiently large population of risks to reduce the variability of the expected outcome.

### 32 Management of Capital

The Group's objectives when managing capital are (i) to comply with the capital adequacy requirements set by the Central Bank of the Azerbaijan Republic, and (ii) to safeguard the Group's ability to continue as a going concern. Compliance with capital adequacy ratios set by the Central Bank of the Azerbaijan Republic is monitored monthly with reports outlining their calculation reviewed and signed by the Group's Chief Executive Officer and Chief Accountant. These reports are prepared based on balances derived from statutory financial statements. Other objectives of capital management are evaluated annually.

**Capital adequacy requirements of the CBAR** Under the current capital requirements set by the Central Bank of the Azerbaijan Republic banks have to maintain a ratio of regulatory capital to risk weighted assets ("total capital ratio") and a ratio of Tier I capital to risk weighted assets above the prescribed minimum level. As at 31 December 2010, these minimum levels were 12% and 6% respectively (2009: 12% and 6%) The minimum share capital requirement set by the Central Bank of the Azerbaijan Republic was AZN 10,000 thousand (2009: AZN 10,000 thousand).

For the CBAR statutory capital adequacy purposes the amount of the cumulative capital that the Bank manages as at 31 December 2010 is AZN 53,685 thousand (2009: AZN 59,927 thousand). The Bank was in compliance with these CBAR requirements as at 31 December 2010

**Capital adequacy requirements established by the financial covenants stipulated in the term borrowing agreements with the international financial institutions** The Group and the Bank are also subject to minimum capital requirements established by covenants stated in the loan agreement with Black Sea Trade and Development, including capital adequacy levels calculated in accordance with the requirements of the Basle Accord, as defined in the International Convergence of Capital Measurement and Capital Standards (updated April 1998) and Amendment to the Capital Accord to incorporate market risks (updated June 2006), commonly known as Basel I. The composition of the Group's consolidated capital calculated in accordance with the Basel Accord is as follows:

<i>In thousands of Azerbaijani Manats</i>	2010	2009
<b>Tier 1 capital</b>		
Share capital	53,685	41,712
Share premium	3,464	3,464
(Accumulated loss)/Retained earnings	(1,752)	1,084
Current year profit	8,361	9,043
<b>Total tier 1 capital</b>	<b>63,758</b>	<b>55,303</b>
<b>Tier 2 capital</b>		
Revaluation reserves	3,049	3,143
Revaluation reserves - available for-sale investment	118	149
<b>Total tier 2 capital</b>	<b>3,167</b>	<b>3,292</b>
<b>Total capital</b>	<b>66,925</b>	<b>58,595</b>
<b>Share capital requirement (minimum 2010: AZN 10,000 thousand; 2009: AZN 10,000 thousand)</b>	<b>53,685</b>	<b>41,712</b>
<b>Total capital ratio</b>	<b>17%</b>	<b>15%</b>
<b>Tier I Capital to risk weighted assets</b>	<b>16%</b>	<b>14%</b>

The Group has complied with externally imposed capital requirement throughout 2010 and 2009.

The Group made certain changes in presentation of capital adequacy calculations in this consolidated financial statement as at 31 December 2010 in comparison with the consolidated financial statements as at 31 December 2009. Management believes that, these changes in the presentation did not have any material impact on the presentation of financial position or the performance of the Group as at 31 December 2010 and 31 December 2009, and for the years then ended.

### 33 Contingencies and Commitments

**Legal proceedings.** From time to time and in the normal course of business, claims against the Group are received. Based on its own estimates and both internal and external professional advice, management is of the opinion that no material losses will be incurred in respect of claims and, accordingly, no provision has been made in these consolidated financial statements.

**Tax legislation.** Azerbaijani tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation, as applied to the transactions and activity of the Group, may be challenged by the relevant state authorities. Recent events within the Republic of Azerbaijan suggest that the tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

Management have assessed whether capital transactions involving the Bank's own shares may give rise to non-sales income in the hands of the Group that is subject to income tax in accordance with the Tax Code of the Republic of Azerbaijan. Management firmly believe that such transactions, for example, the issuance by the Group of new shares giving rise to share premium, are not within the scope of the Tax Code and therefore not required to be included in the Bank's income tax calculation. Accordingly, the Bank has not paid or accrued any income tax in relation to such transactions that have resulted in a total share premium account of AZN 3,464 thousand as at 31 December 2010 (2009: AZN 3,464 thousand).

Tax liabilities arising from inter-company transactions are determined, using actual transaction prices. It is possible with the evolution of the interpretation of the transfer pricing rules in the Republic of Azerbaijan and the changes in the approach of the Azerbaijani tax authorities, that such transfer prices could potentially be challenged in the future. Given the brief nature of the current Azerbaijani transfer pricing rules, the impact of any such challenge cannot be reliably estimated; however, it may be significant.

Management believes that its interpretation of the relevant legislation is appropriate and the Group's tax, currency legislation and customs positions will be sustained. Accordingly, at 31 December 2010 no provision for potential tax liabilities had been recorded (31 December 2009: no provision).

**Capital expenditure commitments.** The Group has also contractual commitment in respect of acquisition of new T24 core banking system software AZN 473 thousand (2009: AZN 502 thousand).

The Group has already allocated the necessary resources in respect of these commitments. The Group believes that future net income and funding will be sufficient to cover this and any similar such commitments.

**Operating lease commitments.** At 31 December 2010 and 2009, the Group has no operating lease commitments under non-cancellable operating leases.

### 33 Contingencies and Commitments (Continued)

**Compliance with covenants.** The Group is subject to certain covenants related to borrowings from Black Sea Trade and Development Bank. Non-compliance with such covenants may result in negative consequences for the Group, including growth in the cost of borrowings and the timing of repayment of existing facilities. Management believes that during the period the Group have substantially complied with the covenants that were in force, however, a number of exceptions have been identified as at 31 December 2010, and in some cases the breaches have also been in effect throughout the year.

Details of the breaches identified as at 31 December 2010 are as follows:

- a) Ratio of liquid assets to short-term liabilities - as at 31 December 2010, the Group's liquidity ratio was 31.28% (31 December 2009: 43%), lower than the 50% level specified in the loan agreement;
- b) Ratio of capital to risk-weighted assets - as at 31 December 2010, the Group's ratio was 13.97% (31 December 2009: 14.76%), lower than the 14.5% level specified in the loan agreement.
- c) Ratio of loans in arrears for more than thirty (30) days to all loans in to the Borrower's portfolio - as at 31 December 2010, the Group's ratio was 28.84% (31 December 2009: 67.48%), greater than the 5% level specified in the loan agreement.
- d) Ratio of operating expenses to operation results – as at 31 December 2010, the Group's ratio was 80.40% (31 December 2009: 37.93%), higher than the 65% level specified in the loan agreement.

The total borrowings affected by the breach of the covenant related to the liquidity ratio were AZN 3,715 thousand as at 31 December 2010 (31 December 2009: AZN 4,817 thousand). In accordance with the loan agreement, the borrowings are classified as due and/or repayable on demand in the liquidity disclosures in Note 30.

Accordingly, the borrowings impacted have been reclassified to being on demand within these consolidated financial statements. Management believes that the Group is in compliance with all other covenants as at 31 December 2010.

**Credit related commitments.** The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit, which represent irrevocable assurances that the Group will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans. Documentary and commercial letters of credit, which are written undertakings by the Group on behalf of a customer authorising a third party to draw drafts on the Group up to a stipulated amount under specific terms and conditions, are collateralised by the underlying shipments of goods, to which they relate, or cash deposits and, therefore, carry less risk than a direct borrowing.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Group is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments since most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Group monitors the term to maturity of credit related commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments. Outstanding credit related commitments are, as follows:

<i>In thousands of Azerbaijani Manats</i>	2010	2009
Import letters of credit	3,832	7,303
Guarantees issued	8,539	1,402
Undrawn credit	2,198	290
Less: Provision for credit related commitments	(291)	(176)
<b>Total credit related commitments</b>	<b>14,569</b>	<b>8,819</b>

### 33 Contingencies and Commitments (Continued)

Movement in the provision of credit related instruments are as follows:

<i>In thousands of Azerbaijani Manats</i>	
Provision on 1 January 2009	-
Provision during the year	176
<b>Total provision credit related commitments on 31 December 2009</b>	<b>176</b>
Provision on 1 January 2010	176
Provision during the year	115
<b>Total provision credit related commitments at 31 December 2010</b>	<b>291</b>

The total outstanding contractual amount of undrawn credit lines, letters of credit, and guarantees does not necessarily represent future cash requirements, as these financial instruments may expire or terminate without being funded. The fair value of credit related commitments was AZN 244 thousand at 31 December 2010 (2009: AZN 107 thousand). Credit related commitments are denominated in the following currencies:

<i>In thousands of Azerbaijani Manats</i>	2010	2009
Azerbaijani Manats	7,876	5,689
US Dollars	2,083	2,103
Euro	4,610	1,203
<b>Total</b>	<b>14,569</b>	<b>8,995</b>

### 34 Fair Value of Financial Instruments

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

The estimated fair values of financial instruments have been determined by the Group, using available market information, where it exists, and appropriate valuation methodologies. However, judgement is necessarily required to interpret market data to determine the estimated fair value. The Republic of Azerbaijan continues to display some characteristics of an emerging market and economic conditions continue to limit the volume of activity in the financial markets. Market quotations may be outdated or reflect distress sale transactions and, therefore, not represent fair values of financial instruments.

Management has used all available market information in estimating the fair value of financial instruments.

**Financial instruments carried at fair value.** Investment securities available for sale are carried on the consolidated balance sheet at their fair value. Cash and cash equivalents are carried at amortised cost, which approximates current fair value.

Fair values of available for sale securities have been fair valued by the Group based on financial data of the investees. Valuation techniques required certain assumptions that were not supported by observable market data. Changing any such used assumptions to a reasonably possible alternative would not result in a significantly different profit, income, total assets or total liabilities.



## 34 Fair Value of Financial Instruments (Continued)

**Loans and receivables carried at amortised cost.** The fair value of floating rate instruments is normally their carrying amount. The estimated fair value of fixed interest rate instruments is based on estimated future cash flows expected to be received discounted at current interest rates for new instruments with similar credit risk and remaining maturity. Discount rates used depend on currency, maturity of the instrument and credit risk of the counterparty and were, as follows:

	2010	2009
<i>Due from other banks – Note 8</i>		
Short-term placements with other banks with original maturities of more than three months	13% to 20% p.a.	12% to 20% p.a.
<i>Loans and advances to customers – Note 9</i>		
Corporate loans	5% to 48% p.a.	5% to 48% p.a.
Loans to individuals - consumer loans	3% to 50% p.a.	3% to 44% p.a.
Loans to individuals – entrepreneurs	7% to 48% p.a.	5% to 56% p.a.
Mortgage loans	3% to 28% p.a.	3% to 25% p.a.

Refer to Notes 8 and 9 for the estimated fair values of due from other banks and loans and advances to customers, respectively.

**Liabilities carried at amortised cost.** The fair value of fixed interest rate instruments with stated maturity, for which a quoted market price is not available, was estimated based on expected cash flows discounted at current interest rates for new instruments with similar credit risk and remaining maturity. The fair value of liabilities repayable on demand or after a notice period ("demandable liabilities") is estimated as the amount payable on demand, discounted from the first date that the amount could be required to be paid. Refer to Notes 16, 17, 18 and 19 for the estimated fair values of due to other banks, customer accounts, debt securities in issue and term borrowings, respectively.

**Analysis by fair value hierarchy of financial instruments carried at fair value.**

For financial instruments carried at fair value, the level in the fair value hierarchy into which the fair values are categorised are as follows:

	2010			2009		
	Quoted price in an active market (Level 1)	Valuation technique with inputs observable in markets (Level 2)	Valuation technique with significant non-observable inputs (Level 3)	Quoted price in an active market (Level 1)	Valuation technique with inputs observable in markets (Level 2)	Valuation technique with significant non-observable inputs (Level 3)
<i>In thousands of Azerbaijani Manats</i>						
<b>FINANCIAL ASSETS</b>						
<i>Investment securities available for sale</i>						
- Milli kart	-	-	400	-	-	400
- Baku Stock Exchange	-	-	60	-	-	60
- Visa	118	-	-	149	-	-
- Other	275	-	-	-	-	-

**35 Reconciliation of Classes of Financial Instruments with Measurement Categories**

For the purposes of measurement, IAS 39, *Financial Instruments: Recognition of Measurement*, classifies financial assets into the following categories: (a) loans and receivables; (b) available for sale financial assets; (c) financial assets held to maturity and (d) financial assets at fair value through profit or loss ("FVTPL"). Financial assets at fair value through profit or loss have two subcategories: (i) assets designated as such upon initial recognition, and (ii) those classified as held for trading. The following table provides a reconciliation of classes of financial assets with these measurement categories.

<i>In thousands of Azerbaijani Manats</i>	<b>Loans and receivables</b>		<b>Available for-sale assets</b>		<b>Total</b>	
	<b>2010</b>	<b>2009</b>	<b>2010</b>	<b>2009</b>	<b>2010</b>	<b>2009</b>
<b>Assets</b>						
<b>Cash and cash equivalents</b>	45,242	47,897	-	-	45,242	47,897
<b>Mandatory Reserves</b>	1,102	837	-	-	1,102	837
<b>Due from other banks:</b>	5,947	6,980	-	-	5,947	6,980
<b>Loans and advances to customers</b>						
- Corporate loans	232,084	253,357	-	-	232,084	253,357
- Loans to individuals - consumer loans	25,586	39,324	-	-	25,586	39,324
- Loans to individuals - entrepreneurs	9,930	19,055	-	-	9,930	19,055
- Mortgage loans	85,847	30,773	-	-	85,847	30,773
<b>Investment securities available for sale</b>	-	-	853	609	853	609
<b>Other investment securities</b>	12,979	2,336	-	-	12,979	2,336
<b>Other financial assets:</b>						
- Restricted cash	1,624	2,204	-	-	1,624	2,204
- Fee and commission receivables	373	669	-	-	373	669
- Receivables from shareholders	1,197	-	-	-	1,197	-
- Settlements with operators of payment systems	839	341	-	-	839	341
- Insurance premium receivable	-	80	-	-	-	80
- Credit and debit cards receivables	-	46	-	-	1,197	46
- Other receivables	122	-	-	-	122	-
<b>Total financial assets</b>	<b>422,872</b>	<b>403,899</b>	<b>853</b>	<b>609</b>	<b>423,725</b>	<b>404,508</b>
<b>Non-financial assets</b>					<b>66,003</b>	<b>45,698</b>
<b>Total assets</b>					<b>489,728</b>	<b>450,206</b>

All of the Group's financial liabilities are carried at amortised cost.

### 36 Related Party Transactions

Parties are generally considered to be related if the parties are under common control or one party has the ability to control the other party or can exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

At 31 December 2010, the outstanding balances with related parties were as follows:

<i>In thousands of Azerbaijani Manats</i>	Significant shareholders	Key management personnel	Other related parties
Gross amount of loans and advances to customers (contractual interest rate: 0% - 26% p.a.)	-	23	2,254
Impairment provisions for loans and advances to customers at 31 December	-	-	223
Receivables from shareholders	1,078	-	119
Customer accounts (contractual interest rate: 12% - 16% p.a.)	-	7	610
Debt securities in issue (contractual interest rate: 14% p.a.)	2,000	-	-

The income and expense items with related parties for the year 2010 were as follows:

<i>In thousands of Azerbaijani Manats</i>	Other significant shareholders	Other related parties
Interest income	-	75
Interest expense	120	25
Rental payments for lease of premises	-	94

At 31 December 2009, the outstanding balances with related parties were, as follows:

<i>In thousands of Azerbaijani Manats</i>	Significant shareholders	Key management personnel	Other related parties
Gross amount of loans and advances to customers (contractual interest rate: (0% - 26% p.a.)	73	53	2,291
Impairment provisions for loans and advances to customers at 31 December	1	-	226
Customer accounts (contractual interest rate: 12% - 16% p.a.)	27	1	224
Debt securities in issue (contractual interest rate: 14% p.a.)	2,000	-	-
Purchase of premises	-	-	2,400

The income and expense items with related parties for the year 2009 were, as follows:

<i>In thousands of Azerbaijani Manats</i>	Other significant shareholders	Key management personnel	Other related parties
Interest income	-	7	540
Interest expense	1,080	-	-
Fee and commission income	-	-	1

Key management compensation is presented below:

<i>In thousands of Azerbaijani Manats</i>	2010	2009
<i>Short-term benefits:</i>		
- Salaries	355	379
<b>Total</b>	<b>355</b>	<b>379</b>

### 37 Events After the End of the Reporting Period

During March, 2011 the Group attracted long-term funds from a group of individuals in the total amount of AZN 25,819 thousand, with market interest rates and a maturity of 6 to 8 years.

On March 2011 Group capitalised its profit and issued an additional 11,070 ordinary shares with a nominal value of AZN 1,000 per share through a primary registration at the Baku Stock Exchange. As a result, the allocation of shares following this transaction was as follows: Mr. Etibar Aliyev – 9,713 shares; Kazimir – 6,476 shares; and World Wines – 48,566 shares.