Original

EBS Mortgage Finance Unlimited

Directors' Report and Financial Statements

Year Ended 31 December 2012

Directors' report and financial statements

Contents

Directors and other information

DIRECTORS

Denis Holland	Independent Non-Executive Director and Chairman
William Cunningham	Independent Non-Executive Director
Fidelma Clarke	Group Non-Executive Director
Gerry Gaffney	Executive Director
Owen Purcell	Executive Director (Managing Director)

SECRETARY	Sarah McLaughlin
REGISTERED OFFICE	2 Burlington Road Dublin 4
REGISTERED NUMBER	463791
SOLICITORS	Helen Dooley Group General Counsel Allied Irish Banks, p.l.c. Bankcentre Ballsbridge Dublin 4 Ireland
BANKERS	EBS Limited 2 Burlington Road Dublin 4 Ireland BNP Paribas Ireland 5 George's Dock International Financial Services Centre Dublin 1 Ireland

DIRECTORS' REPORT

The Directors present their report and audited accounts for the year ended 31 December 2012. A statement of Directors' responsibilities in relation to the financial statements appears on page 11.

ACTIVITIES OF THE COMPANY

EBS Mortgage Finance ('the Bank'), an unlimited company, obtained an Irish banking licence under the Irish Central Bank Act, 1971 (as amended) and was registered as a designated mortgage credit institution under the Asset Covered Securities Act, 2001 on 30 October 2008. The Bank is a wholly owned subsidiary of EBS Limited ('EBS' or 'parent') and a member of the EBS Group (the 'Group'). The EBS Group is a wholly owned subsidiary of Allied Irish Banks p.l.c., ('AIB p.l.c.' or 'AIB Group'). The Bank is regulated by the Central Bank of Ireland.

The purpose of the Bank is to issue Mortgage Covered Securities in accordance with the Asset Covered Securities Act, 2001 and the Asset Covered Securities (Amendment) Act 2007 (the 'Asset Covered Securities Acts'). The Bank does not sell mortgage loans directly to the public. It has an origination agreement with EBS whereby EBS continues to sell mortgage loans directly to the public and subsequently transfers loan portfolios to the Bank for an appropriate consideration.

The Bank was incorporated on 30 October 2008 and commenced trading on 1 December 2008. During the period from this date to the end of 2011, EBS sold €8.3bn of residential loans to the Bank and in turn the Bank issued a series of covered bonds. The Bank did not purchase any loans from EBS during 2012. In 2012 the Bank sold a €0.4bn portfolio of retail buy to let loans as part of the Group deleveraging of non core assets as committed to under the Financial Measures Programme in 2011. During 2012, the Bank re-purchased bonds with a nominal value of €0.5bn from EBS. In November 2012 one externally held covered bond with a nominal value of €1bn matured, the Bank replaced this bond with 3 new bonds with a total nominal of €1bn which were subscribed for in full by EBS. At the end of 2012, the total nominal value of covered bonds issued was €3.2bn of which €0.1bn (2011: €1.1bn) were subscribed for by external bondholders and remainder were subscribed for in full by EBS.

A number of the Bank's operational and support activities are outsourced to EBS under a Managed Services Agreement. EBS, as service provider for the Bank, originates residential mortgage loans through its retail network in the Republic of Ireland, services the mortgage loans, and provides inter-company funding as well as a range of other support services. Bank employees perform those specialist roles which arise as a result of the specific designation of the Bank as a designated mortgage credit institution.

Governance is exercised through a Board of Directors comprising 2 executive and 3 non-executive directors, the 2 executive directors and 1 non executive are employees of EBS.

In accordance with the Asset Covered Securities Acts, the Cover-Asset Monitor, Mazars, monitors compliance with the Acts and reports independently to the Central Bank of Ireland.

The Bank is a covered institution within the meaning of the Government Guarantee Scheme ('the Scheme') and stood specified under the Credit Institutions (Financial Support) (Specification of Institutions) Order 2008 (Statutory Instrument No. 416 of 2008) ('CIFS') for the period 30 September 2008 to 29 September 2010. The Bank is not a participating institution under the Credit Institutions (Eligible Liabilities Guarantee) Scheme 2009 which came into effect on 9 December 2009.

DIRECTORS' REPORT (continued)

As a separately licensed credit institution, the Bank's corporate governance practices also reflect the relevant provisions of the Central Bank Code. Corporate Governance in the Bank is exercised through a Board of Directors and a senior management. The Board's policy is to comply with the highest standards of corporate governance as set out in the Central Bank Code. The Bank is required to submit a compliance statement to the Central Bank confirming compliance with the Central Bank Code during 2013.

The Bank is currently a participating institution under the National Asset Management Agency Act 2009. However, there were no mortgage loans transferred under the terms of the Act.

RESULTS FOR THE YEAR ENDED 31 DECEMBER 2012

The Income Statement for the year ended 31 December 2012 and the Statement of Financial Position at that date are set out on pages 72 and 73.

The Bank reported a loss before taxation of €90m for year ended 31 December 2012 (31 December 2011: Loss before taxation €79m). The reported loss is mainly attributable to the loss on sale of a portfolio of residential loans of €152m in 2012, offset by the gain on the repurchase of debt securities in issue of €54m.

Net Interest Income

Net interest income is up €61m or 103%.

Total interest income amounted to €322m in 2012 (2011: €236m). Interest income mainly comprises of interest income from mortgage assets of €285m (2011: €224m) which increased by 27% from 2011. This is mainly due to the additional interest earned in 2012 in respect of the €2.4bn of residential mortgages purchased from EBS in November 2011. Interest income also includes income derived as a result of amortisation of fair value discount on loans and advances to customers of €37m (2011: €11m).

Total interest expense amounted to €202m (2011: €177m). Interest expense consists of interest on inter-company funding from EBS of €44m (2011: €73m) which decreased mainly as a result of a lower market interest rates applying to the inter-company loan and lower average balance provided by EBS. Interest expense also includes interest on debt securities of €76m (2011: €61m) which increased as a result of the interest rate movements and higher average balances of debt securities in issue during the year. The other component of interest expense is amortisation of fair value discount on debt securities in issue of €82m (2011: €39m) which increased in 2012 due to the full year amortisation of the fair value discount on €1.25bn of debt securities issued in November 2011. In 2011 interest expense also included €4m in respect of an acceleration of fair value premium on loans and advances to customers.

Net interest income was €120m (2011: €59m) for the year generating a net interest margin of 172bps (2011: 92bps).

Net Trading Expense

Net trading expense is up €6m.

Net trading expense of €10m (2011: €4m) comprises net interest receivable or payable on derivatives (interest rate swaps) held at fair value through the Income Statement and hedge ineffectiveness. The movement year on year is mainly due to the movement in interest rates and an increase in average swap nominal value due to the purchase of additional loans in November 2011.

Other Operating Losses

Other operating losses are up by €98m.

Other operating losses comprise the loss on sale of residential loans of €152m in 2012 (2011:nil) and profit on repurchase of securities of €54m (2011: nil).

DIRECTORS' REPORT (continued)

Operating Expense
Operating expenses are up by €2m.
Operating expenses which comprise direct costs and a service fee charge from EBS amounting to €8m (2011: €6m). The increase of 33% or €2m is due the overall increase of the Bank's loan book in 2012 following the purchase of €2.4bn of residential loans from EBS at the end 2011.

Credit Provision
The impairment provision charge in 2012 is €94m down from €128m in 2011.
Total provisions (excluding unearned income provisions) held at December 2012 amount to €244m 2011: €171m) Total provisions (including unearned income provisions) held at December 2012 amount to €249m (2011: €172m) of which €205m were specific and €44m were collective. This provided 3.7% coverage on total loans (2011: 2.3%).

Further detail can be found in the Risk Management Report. The impairment charges on loans and advances to customers are detailed in note 8.

Loans and advances to customers
Loans and advances to customers as at 31 December 2012 amounted to €6.4bn (2011: €7.2bn). The decrease from 2011 is primarily due to the sale of mortgage assets with a carrying value of €0.4bn on 01 October 2012 and higher loan impairment provisions €0.1bn.

Funding
The funding of the mortgage assets from EBS is in part through an inter-company loan facility from EBS, which amounted to €3.3bn at 31 December 2012 (2011: €3.6bn).

Debt securities in issue
During the year the Bank re-purchased bonds with a nominal value of €0.5bn from EBS which resulted in an overall re-purchase gain of €54m in 2012.

In November 2012 one externally held covered bond with a nominal value of €1bn matured, the Bank replaced this bond with 3 new bonds with a total nominal of €1bn which were subscribed for in full by EBS. The bonds were recognised on the Statement of Financial Position at a value of €984.8m representing the Day 1 fair value of the bonds. The discount is being amortised through the Income Statement over the life of the bonds.

As at 31 December 2012, the total nominal amount of principal outstanding in respect of mortgage covered securities was €3.2m (2011: €3.6bn) of which €0.1bn (2011: €1.1bn) was held by third parties and €3.1bn (2011: €2.5bn) by EBS.

Share Capital
The share capital of the Bank consists of 476,540,000 €1 ordinary shares issued to EBS (2011: 476,540,000 €1 ordinary shares).

DIRECTORS' REPORT (continued)

Capital ratios

For 2012, the capital ratios are calculated in accordance with the Capital Requirements Directive.

	2012 €m	2011 €m
Core Tier 1 Capital	351	429
Non Core Tier 1 Capital	-	-
Tier 1 Capital	351	429
Tier 2 Capital	44	8
Total Capital	395	437
Risk Weighted Assets	3,538	3,803
Total Capital Ratio	11.1%	11.5%
Tier 1 Ratio	9.9%	11.3%
Core Tier 1 Ratio	9.9%	11.3%

At 31 December 2012 the total capital ratio was 11.1% (2011: 11.5%) and the tier 1 ratio was 9.9% (2011: 11.3%). Both of these are above Regulatory Capital minimum. Further information in relation to Regulatory Capital is set out in note 19.

BUSINESS REVIEW AND FUTURE DEVELOPMENTS

The residential mortgage market is a key component of the overall EBS strategy and access to funding is a key requirement to deliver on this strategy. As a result EBS established the covered bond bank, EBS Mortgage Finance, in 2008 with the purpose of enabling funding to be raised in the form of covered bonds and to strengthen the liquidity position of the EBS Group.

Market conditions in peripheral European covered bond jurisdictions improved consistently in the second half of 2012 and supported the issue of bonds in primary markets as evidenced by the issue by AIB Mortgage Bank of bonds with a tenor of 3 Years and a nominal value of €0.5bn prior to the end of 2012. The improved position of the Irish sovereign and stabilisation of the fiscal position of the State and macro economy as a whole resulted in the stabilisation of Ireland's sovereign rating, institutional bank ratings and ultimately covered bond ratings. In November 2012 the Bank's covered bond programme rating was upgraded to 'A' by Fitch Ratings, the Moody's Investor Services rating was unchanged at Baa3. The Bank did not issue any bonds to external investors during 2012.

As part of its mandate to support the EBS Group's liquidity position the Bank did issue covered bonds amounting to €1bn during 2012. The bonds which meet the ECB eligibility criteria for use as collateral in their open market operations were subscribed for in full by EBS and used to access such funding from the ECB.

On 1 October 2012 the Bank sold residential buy to let mortgage assets with a total debt value of €0.4bn to EBS at a fair value consideration amount of €0.2bn.

The residential mortgage market continued to experience low levels of demand due to weak consumer sentiment, uncertainty regarding the future direction of house prices and a limited supply of mortgage credit. This has resulted in 2012 mortgage volumes continuing to remain at low levels. However having contracted for five successive years the housing market showed positive signs in the second half of 2012. According to the CSO house price index, average residential property prices reduced by 4.5% in 2012 and 50% from peak, this compares to a decline of 16.7% recorded in the twelve months to December 2011. Supply of mortgage credit, much like 2011, was provided in the main by AIB

DIRECTORS' REPORT (continued)

Group and Bank of Ireland. A lower interest rate environment and reduction in house prices means that affordability levels for new home buyers continued to improve which combined with announcements of increased mortgage lending by a number of banks points towards increased activity in the mortgage market in 2013.

We expect the operating environment to remain difficult throughout 2013. The Irish economy continues to face difficult challenges. While critical elements of the economy such as the export sector are performing strongly, and Government finances have stabilised, the current phase of economic contraction, falling employment and property asset values have yet to stabilise.

RISK MANAGEMENT

The risk management framework provides a firm-wide definition of risk and lays down the principles of how risk is to be identified, assessed, measured, monitored and controlled / mitigated and the associated allocation of capital against same. The Bank categorises risks under a number of headings namely, strategic, operational, compliance and financial (including credit, liquidity and market) risks. Together, these form the Bank's Risk Universe. This helps the Bank to assess and manage risk on an enterprise wide, holistic basis. The Risk Universe is continuously reviewed and updated reflecting the changing risk environment and was reviewed by the Board during 2012. Each of these risks are fully described in the Risk Management Report.

Also further information in relation to the Risk factors affecting the Group are set out in the Risk Management Report.

GOING CONCERN

The Directors have prepared these financial statements on the going concern basis which assumes that the Bank will continue in operational existence for the foreseeable future having adequate funds to meet obligations as they fall due. EBS Mortgage Finance is dependent on its ultimate Parent, Allied Irish Banks, p.l.c. for continued funding and is therefore dependent on the going concern status of the Parent.

The financial statements of Allied Irish Bank p.l.c (the "AIB Group") have been prepared on a going concern basis as the Directors of the AIB Group are satisfied, having considered the risks and uncertainties impacting the AIB Group, that it has the ability to continue in business for the foreseeable future. In making its assessment, the Directors have considered a wide range of information relating to present and future conditions. These have included financial plans, cash flow and funding forecasts, capital resources projections, all of which have been prepared under base and stress scenarios. The AIB Group Directors have also considered the AIB Group's ability to access funding and liquidity. In addition, the AIB Group have considered the commitment of support provided to AIB by the Irish Government through the programme for restructuring the Irish banking system with AIB designated as one of the two 'Pillar Banks'.

The Directors of AIB Group are satisfied based on the clarity of confirmations received from the Central Bank of Ireland and public announcements by ECB, EU and IMF that in all reasonable circumstances the required liquidity and funding from the Central Bank/ ECB will be available to the Group during the period of assessment.

On the basis of the continued availability of funding from Allied Irish Banks, p.l.c to EBS Mortgage Finance, the Directors of the Bank consider that it is appropriate to prepare the financial statements on a going concern basis at this time.

DIRECTORS' REPORT (continued)

DIVIDENDS
The Directors do not recommend payment of a dividend in the year to 31 December 2012 (2011: Nil).

DIRECTORS' AND SECRETARY'S INTEREST IN SHARES
The beneficial interest of the Directors and the Secretary in office at 31 December 2012 and of their spouses and minor children in the shares of group companies are set out below. The shares referred to are €0.01 ordinary shares in ("AIB"), the holding company.

Ordinary Shares

	31 December 2012	31 December 2011*
Directors:		
Denis Holland	Nil	Nil
Fidelma Clarke	Nil	Nil
William Cunningham	Nil	Nil
Gerry Gaffney	Nil	Nil
Owen Purcell	Nil	Nil
Secretary:		
Sarah McLaughlin	377	377

** or date of appointment, if later.*

DIRECTORS' REPORT (continued)

Share options
Details of the Directors' and the Secretary's options to subscribe for ordinary shares in AIB, are given below. The vesting of these options to the individuals concerned is dependent on Earnings Per Share ("EPS") targets being met by AIB. Subject thereto, the options outstanding at 31 December 2012 are exercisable at various dates between 2013 and 2015. Details are shown in the Register of Directors' and Secretary's Interests, which may be inspected at the Company's registered office.

	31 December 2012	1 January 2012	Options lapsed during 2012	Weighted average subscription price of options outstanding 31 December 2012
Directors:				€
Fidelma Clarke	-	-	-	-
Gerry Gaffney	-	-	-	-
Owen Purcell	-	-	-	-
Secretary				
Sarah McLaughlin	-	-	-	-

Independent Non-Executive Directors do not participate in share option plans. No options were granted or exercised during the year.

Long term incentive plans
There were no conditional grants of awards of ordinary shares outstanding to Executive Directors or the Company Secretary at 31 December 2012.

Independent Non-Executive Directors do not participate in long term incentive plans.

Apart from the interests set out above, the Directors and Secretary and their spouses and minor children have no other interests in the shares of Allied Irish Banks, p.l.c.

There were no changes in the Directors' and Secretary's interests between 31 December 2012 and the reporting date.

Directors and Secretary

The following Board changes occurred with effect from the dates shown:

- Ms. Dara Deering resigned as Executive Director on 4 January 2012;
- Mr. Fergus Murphy resigned as Executive Director on 21 March 2012;
- Mr. Owen Purcell was appointed Executive Director on 20 June 2012;
- Ms. Audrey Collins resigned as Executive Director on 3 August 2012;
- Ms. Helen Dooley resigned as Company Secretary on 11 September 2012;
- Ms. Sarah McLaughlin was appointed Company Secretary on 11 September 2012;
- Mr. Gerry Gaffney was appointed Executive Director on 3 December 2012.
- Ms. Fidelma Clarke transitioned from an Executive Director to a Group Non-Executive Director on 3 December 2012.

Statement of directors' responsibilities

The directors are responsible for preparing the directors' report and financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law, the directors are required to prepare the Company financial statements in accordance with IFRSs as adopted by the EU and have elected to prepare the financial statements in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Acts 1963 to 2012.

The financial statements are required by law and IFRSs as adopted by the EU to present fairly the financial position and performance of the company; the Companies Acts 1963 to 2012 provide in relation to such financial statements that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation.

In preparing the financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper books of account that disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that its financial statements comply with the Companies Acts 1963 to 2012. They are also responsible for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.

On behalf of the board

Director   Director

Date: 26/3/13   Date: 26/3/13

RISK MANAGEMENT REPORT

1. Introduction

Over the course of 2012, EBS Group (the 'Group') has been aligning and integrating its risk management structures and frameworks with AIB Group. The Group's risk profile remains at an elevated level, driven principally by both the ongoing challenges of the external environment and a number of internal factors, both legacy and reflecting the level of organisational transformation currently underway

The Bank, as a wholly owned subsidiary of the Group has adopted a risk management structure and controls framework consistent with that of EBS Limited ('EBS'). The governance and organisation framework through which the Group manages and seeks where possible to mitigate its risks is described below. The key risk factors to which the Bank is exposed are set out in the section below.

2. Risk Management Framework

The Group assumes a variety of risks in undertaking its business activities. EBS and its subsidiaries (which includes the Bank) defines risk as any event that could damage the core earnings capacity of the Group, increase earnings or cash-flow volatility, reduce capital, threaten business reputation or viability, and/or breach regulatory or legal obligations. The Group recognises that the effective management of risk and its system of internal control is essential to the minimisation of volatility against forecasted financial performance, the preservation of customer value and the achievement of the Group's' strategic objectives. The primary focus of the risk management framework is to ensure that the Group achieves the optimal risk/reward return on any investment of people, time and resources.

The Bank is also subject to the monitoring of specific risks by the CAM as set out in the ACS act.

3. Risk governance and risk management organisation

Risk management in the Bank is supported by a clear risk management governance structure, a clear risk management framework and a significant investment of both senior management and Board time in reviewing the system of internal control. The Board has ultimate responsibility for the governance of all risk taking activity in the Bank. The Group has adopted a 'three lines of defence' framework in the delineation of accountabilities for risk governance. Under the three lines of defence model, primary responsibility for risk management lies with the business line management. The Risk Management Functions (both Group and AIB Group) provide second line of defence, providing independent oversight and challenge to business line managers. The third line of defence is the AIB Group Internal Audit function which provides independent assurance on the effectiveness of the system of internal controls.

Whilst the Board has ultimate responsibility for all risk taking activity within the Bank, it was supported in 2012 by the work of its sub committee, namely the Board Audit, Risk and Compliance Committee ("BARCC"). The BARCC supported the Board in monitoring the integrity of the financial statements, fulfilling its responsibilities in relation to the system of internal control, internal audit and compliance, by overseeing the relationship between the Bank and its external auditors, and discharging statutory duties in respect of relevant laws and regulations. It was also responsible for considering and recommending as appropriate to the Board, acceptance of the Bank's risk management and governance infrastructure, the Bank's material risk policies and risk appetite, risk disclosures in the Annual Report and Accounts and other Prospectus and capital adequacy including internal capital assessment and allocation. Following a review of governance in late 2012, the decision has been taken to merge the responsibilities and membership of the BARCC into the Board, which will continue to meet regularly throughout the year.

The Executive Management Team of the Bank has responsibility for the management of the business as a whole including the origination of mortgages from the Group and those assets which comprise the Cover Pool. It has responsibility for devising and implementing the strategic business plan of the Bank

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and monitoring actual and projected performance including profitability, impairments, capital ratios and adherence to Cover Pool management policy.

3.1 Risk Committees and Functions

The Bank's Asset and Liability Committee (ALCO) was established to monitor the Bank's exposure to key market risks, i.e., liquidity risk, funding risk, interest rate risk, counterparty credit risk and foreign exchange risk. The Committee was responsible in 2012 for asset & liability management, monitoring the adequacy of the liquidity framework and buffers, and for recommending the appropriate funding, liquidity, counterparty credit and market risk policies and plans to the Board for approval. The Committee monitored capital ratios, including projections and oversees the appropriate implementation of the capital policy. Following a mid year review of governenace, the role and responsibility of the Bank's ALCO was assumed back into the Group ALCO.

The Bank is supported in its risk activities by the work of various Group risk committees and by both Group and AIB Group Risk functions. Following a review of governance in late 2012, the various Group risk committees were amalgamated in January 2013 to form an EBS Executive Risk Committee (ERC) The ERC, which meets monthly, reviews and recommends appropriate credit risk, operational risk and regulatory compliance risk management policies for EBS and its subsidiaries, in line with the overall risk appetite of the Group and AIB Group. The Committee is also responsible for monitoring the make up and performance of the loan books and the adequacy of provisions for impaired loans. The evaluation of Counterparty Credit Risk and limit setting is performed at AIB Group level. The Committee monitors the external macro-economic and other factors and new business credit risk trends and projections which serve as a benchmark against which the credit risk appetite of the organisation is evaluated.

The EBS Risk Rating Approval Committee (RRAC), which meets semi annually, is responsible for reviewing and recommending to the Group Board policies on risk model development, validation and use. It is also responsible for the ongoing validation and monitoring of risk rating systems, model performance and model output in terms of forecasting.

The Group and AIB Group Risk functions support the Bank and EBS in developing and maintaining a robust risk management framework, and by providing independence in terms of risk identification, measurement, monitoring and reporting.

Over the course of the second half of 2012, Group Risk functions have either been co-located or integrated with the equivalent functions in AIB Group.

In line with the AIB Group stress testing framework, the Group measures its vulnerabilities to loss under stressed market conditions and considers those results when agreeing financial budgets and on an ongoing basis for monitoring and reviewing risk appetite and risk contingency plans. The stress testing framework, which forms an integral part of the overall governance and risk management culture of the Group, has been developed in line with the European Banking Authority revised guidelines on stress testing which became effective on 1st January 2011. The stress testing program incorporates stress tests at both an individual risk level (bottom up approach) and at a holistic organisation wide level (integrated top down approach) that cover a range of risks and business areas. The stress testing program facilitates the development of risk mitigation or contingency plans across a range of stressed conditions that are used to support the organisation from a risk appetite, capital and liquidity management perspective. Contingency plans also reflect operational response considerations where appropriate.

4. Risk Appetite Statement and Risk Polices

The Bank's risk appetite is defined as the maximum amount of risk that the Bank is prepared to accept in order to deliver on its strategic and business objectives. The Bank maintains its own risk appetite statement ('RAS') which was updated in May 2012 to align with both the Group and AIB Group RAS. The RAS is a blend of qualitative and quantitative limits and triggers linked to the Bank's objectives. The Bank's risk profile is measured against its risk appetite regularly and reported to the Executive Management Team and Board. Material breaches of risk appetite, if they occur, are escalated by the

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Board to the Central Bank. Risk policies and procedures are updated where appropriate to reflect the limits of risk appetite. These policies are closely managed on a day to day basis, and are monitored by the Bank's Executive management team supported by relevant Group and AIB Group Risk functions with oversight provided by the Bank's Executive management team.

5. Risk Factors

EBS' approach to identifying and monitoring the principal risks and uncertainties facing EBS is informed by risk factors. All of EBS' activities, and those of the Bank, involve, to varying degrees, the measurement, evaluation, acceptance and management of risks which are assessed on a company wide basis. Certain risks can be mitigated by the use of safeguards and appropriate systems and actions which form part of EBS' and the Bank's risk management framework, as described below. The principal risks and uncertainties facing the Bank are as follows:

5.1 The Bank's dependence on the EBS and AIB Group

The Bank is dependent on EBS in relation to the origination and to AIB Group in relation to the servicing of Irish residential loans, administration and accounting services, treasury services, hedging arrangements, debt funding, equity and regulatory capital and services relating to the issuance of Mortgage Covered Securities. To meet its funding requirements, the Bank has dependency on EBS and AIB Group. EBS and the AIB Group has accessed a range of central bank liquidity facilities, including at times certain additional liquidity schemes introduced by central banks for market participants during periods of dislocation in the funding markets. In accessing central bank and other secured lending facilities, the EBS and AIB Group has relied significantly on its "Qualifying Liquid Assets" and "Contingent Funding" capacity. The curtailment or non-extension of the Central Bank liquidity facilities currently relied upon by the AIB Group, or the AIB Group's inability to access such facilities would require the AIB Group to seek alternative sources of funding.

The Bank is entirely dependent on EBS who in turn is dependent on the AIB Group to provide the necessary capital resources to meet minimum regulatory requirements. The AIB Group's target capital requirements as determined by the Central Bank under its Prudential Capital Assessment Review (PCAR) are currently core tier 1 ratio of 8.92% in the base scenario and 6% in a stress scenario (excluding a requirement for an additional protective buffer). As at December 2012 the Group achieved a core tier 1 ratio of 15.8% which is significantly above the required level. AIB Group has carried out extensive forward-looking stress tests on its capital adequacy position, including two European Banking Authority (EBA) stress tests carried out in the second half of 2011, the latter of which had a threshold of 9% core tier 1 ratio and included an additional stress on sovereign exposures. The published results of both EBA stress tests confirmed that AIB did not require additional capital. However given the levels of uncertainty in the current economic climate there is the possibility that further losses over and above what is currently forecast could materialise. Were such losses to be significantly greater than currently forecasted, the AIB Group's capital position could be eroded to the extent that it has insufficient capital resources to provide to EBS and in turn to the Bank to meet the Bank's regulatory requirements which is a total solvency ratio of 9%.

5.2 The Group's business may be adversely affected by a further deterioration in economic and market conditions

The deterioration of the Irish economy has significantly adversely affected the Group's financial condition and performance in recent years. Although, following a very deep recession, economic activity had regained some momentum both in Ireland and internationally, global activity has weakened again.

A renewed downturn in the performance of the Irish economy or other relevant economies could further adversely affect the Group's financial condition and results. This could include further reductions in business activity, lower demand for the Group's products and services, reduced availability of credit, increased funding costs, decreased asset values, and additional write-downs and impairment charges. This would have a material adverse effect on the Group's plans for recovery. The Group's financial

Forms integral part of the audited financial statements

performance may also be affected by future recovery rates on assets and the historical assumptions underlying asset recovery rates may no longer be accurate, given the general economic instability.

5.3 General economic conditions continue to be very challenging for mortgage and other lending to customers and increase the risk of payment default

The Group remains heavily exposed to the Irish residential property market. The high level of unemployment, coupled with a general reduction in disposable income (from increased taxes and pay reductions) has had an adverse impact on borrowers' ability to repay loans which is evidenced by the increasing arrears on residential property mortgages.

Furthermore, since 2011 a number of initiatives and regulations were introduced following the Inter-Departmental Working Group on Mortgage Arrears, including the publication of the 'Keane Report', the Code of Conduct on Mortgage Arrears, the Consumer Protection Code 2012 and the 2012 Code of Conduct for Business Lending to Small and Medium Enterprises and the requirement for Mortgage Arrears Resolution Strategies. Collectively, these have led to a need for more sophisticated mortgage arrears management strategies, in particular, the application of forbearance measures which were introduced in 2012. The impact of these measures has yet to be seen, but it does increase the risk of potential loan losses which the Group would not otherwise incur as it may lead to a lack of willingness (as opposed to ability) to repay loans. Furthermore, there is a risk that the reforms of Irish bankruptcy law may result in more customers choosing this as a debt solution.

Overall, there is an increased risk of further impairment to the Group's residential mortgage and commercial property loan portfolios, leading to higher costs, additional write-downs and lower profitability for the Group.

5.4 The depressed Irish property prices may give rise to increased losses by the Bank

Since the beginning of 2007, the Irish residential property market has undergone a material negative correction both in property prices and lending activity.

The Bank's exposure to credit risk is exacerbated when the collateral it holds cannot be realised or is liquidated at prices that are not sufficient to recover the full amount of the loan due to the Bank. This is most likely to occur during periods of illiquidity and depressed asset valuations, such as those currently being experienced.

Any such losses could have a material adverse effect on the Bank's future performance and results. In addition, an increase in interest rates may lead to, amongst other things, further declines in collateral values, higher repayment costs and reduced recoverability which together with the aforementioned risks may adversely impact the Bank's earnings or require an increase in the expected cumulative impairment charge for the Bank.

5.5 Extensive powers continue to be conferred on the Irish Minister of Finance

The Credit Institutions (Stabilisation) Act 2010 conferred extensive powers on the Irish Minister of Finance to direct the affairs of and restructure credit institutions and reorganise their assets and liabilities. Pursuant to the Act, directors are required to act in a manner that is aligned to the interests of the State in the performance of their duties, having regard to public interest considerations specified in the Act. The provisions of the Act were to cease to have effect on 31 December 2012 unless otherwise extended. The Act was extended and remains in effect until the end of 2014, unless further extended in due course.

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5.6 The Bank's business activities must comply with increasing levels of regulatory requirements introduced as a result of failings in financial markets

In 2012 there was an unprecedented level of new regulation issued by both by the Central Bank of Ireland and the EU, through a number of new or revised Codes and Directives:

- The first compliance statement under the Corporate Governance Code for Credit Institutions and Insurance Undertakings which was introduced on 1 January 2011 was required to be submitted. The Code sets out the minimum requirements an institution must meet to promote strong and effective governance; and
- The revised Consumer Protection Code came into effect on the 1 January 2012 with consideration given until the 30 June 2012 for full compliance.

Change programmes were initiated across the Group to implement these new requirements spanning all business areas, processes and systems and the Group is operating fully to these codes now.

The Personal Insolvency Act, which was signed into law in December 2012, provides for the introduction of new non-judicial debt settlement and for amendments to the Bankruptcy Act. It is expected that in quarter 1 2013, the newly established Insolvency Service of Ireland will issue relevant guidelines and publications and that in quarter 2 the Insolvency Service will begin to appoint Personal Insolvency Practitioners. A key risk arises from potential changes in customer behaviour and attitude to debt obligations given that the new legislation allows for the agreed settlement of unsecured debt and the settlement/restructuring of secured debts up to a maximum of €3 million. The inclusion of secured debt in the non-judicial process is unprecedented, and therefore, it is difficult to gauge its impact. While the Personal Insolvency Arrangement ("PIA") requires prior co-operation and engagement by Private Dwelling House ("PDH") borrowers under the MARP process, this requirement does not apply to other secured debtors.

These factors could impact on the potential number of customers applying through the insolvency process, with potential negative consequences for the Group in terms of resourcing, impairment provisions and capital adequacy, with ensuing adverse Government, media and consumer reactions. It is recognised that Personal Insolvency Practitioners ("PIP"), who have yet to be authorised, will play a key role in the effective implementation of the legislation as will the guideline living standards for applicants. While the Insolvency Service has given indications as to its intended approach in relation to these factors, there remains uncertainty that the controls will be adequate to mitigate the downside risk of changes to customer behaviour.

A number of new legislative proposals are currently being considered by the Oireachtas (the Irish National Parliament) including the Central Bank (Supervision and Enforcement Bill) 2011 and the Credit Reporting Bill 2012.

Together with the high level of existing regulations, the challenge of managing regulatory compliance increased substantially in 2012. The changing regulatory standards have posed a concomitant demand on the Bank and it's service providers (EBS and AIB Group) in terms of the deployment of business and IT resources which is expected to continue in 2013. Delivering this level of change has and will continue to place added risk on the Bank and the Group, including the challenge to meet tight delivery timelines in the face of competing priorities and resource demands.

The Bank is subject to financial services laws, regulations and policies. Changes in supervision and regulation in or applying to Ireland has and will continue to have a material impact on the Bank's business, products offered and the value of its assets.

Future changes in government policy, central bank monetary authority policy, EU/Eurozone policies, legislation or regulation or their interpretation relevant to financial services may adversely affect the Bank's product range, funding sources, capital requirements and consequently reported results and financing requirements.

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Any changes in the regulation of selling practices and solvency, funding and capital requirements could have a significant impact on the Bank's results of operations, financial condition and future prospects.

Furthermore, any new regulatory obligations regarding functional and operational arrangements within the Group or AIB Group may also have an adverse impact on the Bank's results, financial conditions and prospects.

6. Risk Disclosures

The risk management framework provides a firm-wide definition of risk and lays down the principles of how risk is to be identified, assessed, measured, monitored and controlled / mitigated and the associated allocation of capital against same. The Bank categorises risks under a number of headings namely, strategic, operational, compliance and financial (including credit, liquidity, market and over collateralisation) risks. Together, these form the Bank's Risk Universe. This helps the Bank to assess and manage risk on an enterprise wide, holistic basis. The Risk Universe is continuously reviewed and updated reflecting the changing risk environment.

Strategic Risk

Strategic risk management encompasses the management of the Bank's reputation and the implications for the Bank's covered bond programme of credit rating movements of either the Bank or the EBS. Strategic risk also encompasses external events which cannot be controlled but which could have a significant impact on the Bank's business such as the domestic macro economic environment, property values, banking sector and covered bond market conditions. Strategic risks are managed and monitored in the main by the Executive Management Team and the Board. Significant developments are reported to the Board directly and to its subcommittee on a regular basis.

Operational Risk

Operational risk is the current or prospective risk of loss arising from inadequate or failed internal processes or systems, human error or external events.

EBS Group Operational Risk is responsible for supporting the Bank in the management of Operational Risk. EBS Mortgage Finance has adopted relevant EBS Group Operational risk policies. These policies have been aligned with AIB Group Policies over the course of 2012. The core focus of Operational risk management is the oversight of outsourced service activities related to the mortgage collateral of the Bank, management of the collateral pool in accordance with the requirements of the ACS Act, third party relationship management, business continuity management, fraud prevention, maintenance of efficient business process and operating practices, employee development and key person risk.

Regulatory Compliance Risk

Regulatory compliance risk is the risk that the Bank fails to meet its legislative or regulatory requirements as set out by the Central Bank and where applicable, by the European Banking Authority. Compliance independently evaluates adherence to key regulations and updates management via the EBS Executive Risk Committee (ERC). An overall annual plan is developed for the AIB Group which includes EBS Group.

AIB Group Regulatory Compliance is responsible for supporting the Bank in monitoring adherence to its regulatory compliance obligations. EBS adopted the AIB Group regulatory compliance policies in 2012. The core focus of regulatory compliance risk management is on supporting EBS Mortgage Finance's adherence with the requirements of the ACS Act, terms and conditions of its banking license, the Capital Requirements Directive and conditions of the government guarantee scheme.

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Financial Risk
EBS Mortgage Finance has exposure to the following financial risks - credit risk, interest rate risk, liquidity & funding risks.

EBS Treasury is responsible for supporting the Bank in the management of certain financial risks and adherence to legislative requirements specific to Designated Credit Management Institutions including to interest rate risk, foreign exchange risk, duration mismatch and interest coverage.

Over Collateralisation Risk
A significant level of over collateralisation ('OC') is held in the covered asset pool in order to provide adequate protection to bondholders in the event of higher defaults and reducing asset values. The Bank has, as required, increased the nominal OC level during the period in response to the fall in asset values such that the prudent value of the collateral pool as measured in the regulatory OC value of the cover pool exceeds minimum regulatory, contractual and rating agency requirements. The Directors are satisfied that existence and level of over collateralisation provides the Bank with access to sufficient liquidity to enable repayments to be made when they fall due.

The Asset Covered Securities Act also provides protection to the Bondholders in preference to any other creditors in both the Bank and the Society. The Directors are also satisfied that the Bank is protected under the legislation such that it in the event of any parental insolvency that the liabilities due to the Bondholders as secured creditors can be met in priority to un-secured creditors.

6.1 The Bank has exposure to the following risks from its use of financial instruments:

(i) Liquidity risk
(ii) Market risks
(iii) Credit risk.

__Liquidity risk*__
Liquidity risk relates to the ability of EBS Mortgage Finance to meet its on and off balance sheet obligations in a timely manner as they fall due, without incurring excessive cost, whilst continuing to fund its assets and growth therein. As part of the terms of its bank licence approval EBS Mortgage Finance elected to meet its solo prudential liquidity requirements at a Group level which during 2012 was amended to be at an AIB Group Level.

As at the 1st July 2011 EBS was acquired by the AIB Group following instructions from the Minister for Finance on the 31st March 2011. As part of the AIB Group, EBS' liquidity risk has been incorporated into the AIB centralised risk management model in line with AIB' common approach to Treasury Risk management. Under this centralised approach the management of Liquidity and related activities are overseen and controlled by AIB Treasury.

AIB Group Treasury, is responsible for the daily management of liquidity and funding, and their role is to ensure that resources are available at all times to meet EBS' obligations arising from the daily business of the bank. EBS reports its liquidity positions to the Central Bank of Ireland as part of the AIB Consolidated Liquidity Reporting. These risks are monitored and reports on key developments are communicated to the EBS Management team monthly and onwards to the EBS Board on a regular basis via the Chief Risk Officers report.

EBS conducts both regular and ad-hoc funding and liquidity risk stress testing to assess on an ongoing basis the ability of EBS to withstand various idiosyncratic and systemic stress scenarios. Liquidity contingency plans are developed and updated on a continual basis reflecting the results of the stress tests. These activities are conducted in conjunction with AIB Group Asset & Liability Management.

EBS applies the maturity mismatch approach to the management of liquidity following the adoption of this method by the Central Bank of Ireland in July 2007. The overall purpose of a maturity mismatch approach is to ensure that the EBS will have, at any given time, a pool of highly liquid assets capable of

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being converted into cash within four business days, sufficient to cover a certain percentage of foreseeable cash outflows for future periods of time ('time bands'). EBS has conducted stress tests in advance of these expected changes. Funding contingency plans are continually under review in light of unprecedented market and EBS specific events.

Key measures used by EBS for managing liquidity risk are the liquidity ratios, calculated and reported on a daily basis internally to the Treasury Front Office and to AIB Group, on a weekly basis for consolidation into the AIB Group Regulatory Liquidity Reports and on a monthly basis to the EBS Management team and onwards to the Board

In October 2011 the Central Bank revoked the requirement for EBS to comply with the 'Requirements for the Management of Liquidity Risk' regulatory document under Section 9.2 of that document. Whereupon the EBS Liquidity Ratios would henceforth be reflected in the AIB Group Consolidated Liquidity Reports.

Market Risk*

Market risk is the risk that changes in market prices, such as interest rate, and credit spreads (funding risk) will affect the Bank' income. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk. EBS is in the process of aligning the measurement methods and reporting of its market risk exposures to the AIB Group.

The Bank is not allowed to engage in proprietary trading as per the conditions of the Asset Covered Securities Act (ACS Act) and it's license. EBS Treasury manages non trading Interest Rate Risk using gap and sensitivity analysis in conjunction with AIB Group Treasury. Derivatives such as interest rate swaps are used to hedge these market risks. The EBS Management team monitors these risks monthly and reports on key developments to the Board on a regular basis.

Interest rate risk is the risk that changes in interest rates will affect the Bank's income or the value of its holdings of financial instruments. The objective of interest rate risk management is to manage and control interest rate risk exposures in accordance with the requirements of the ACS act and internal parameters.

The Bank has outsourced the measurement and reporting management of its interest rate risk to the EBS Group. EBS Treasury Risk measures and manages these risks using gap and sensitivity analysis. Derivatives such as interest rate swaps are used by the Bank for hedging purposes (reducing risk) only. The EBS Management team is responsible for monitoring how interest rate risk is managed and ensuring that EBS Mortgage Finance policy is adhered to.

Credit Risk*

Credit risk is the risk of financial loss to EBS Mortgage Finance if a customer or counterparty to a financial instrument fails to meet its contractual obligations.

The Bank's core focus in relation to credit risk management relates to the management of asset quality and counterparty credit risk. All mortgage credits purchased by the Bank and held as assets must be originated by EBS in accordance with lending policies approved by the Board of directors of EBS as applicable at the time of origination of the loan as reflected in the Wholesale Mortgage Origination Agreement between EBS and the Bank.

Credit risk management at EBS Group level is supported by an appropriate governance structure with separation of function between the sourcing and approval of business, the issuing of funds, loan management and independent review and monitoring. Given the continued deterioration in credit quality throughout 2012 in both the retail and commercial markets, both credit management and credit risk management have been a key area of focus over the past year. Resourcing, structures, policies and processes continue to be reviewed in order to ensure that EBS is best placed to manage asset quality in this severe downturn. The EBS Executive Risk Committee (ERC) is responsible for reviewing

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appropriate credit risk management structures, forbearance strategies and policies in line with the credit risk appetite of the Group and AIB Group and for monitoring the performance of the book.

The EBS Risk Analytics team is responsible for the development and ongoing validation of credit risk rating models which are used to assess credit applications and to support a robust capital adequacy assessment process, and for independently monitoring the quality of EBS Mortgage Finance's loan assets. Credit impairment provisions are in line with International Financial Reporting Standards, the calculation and management of which are outsourced to EBS.

The Group conducts both regular and ad-hoc credit risk stress testing to assess on an ongoing basis the ability of the Group to withstand various idiosyncratic and systemic stress scenarios. Credit contingency plans are developed and updated on a continual basis reflecting the results of the stress tests.

Given the economic environment, the Group conducts a quarterly assessment of impairment provisions, assisted by the Risk Analytics and Credit teams and evaluated by the Executive Risk Committee.

Claims against Banks and Credit Institutions are restricted to overnight deposits with counterparties that meet minimum legislative requirements.

Maximum exposure to credit risk*

The following table shows the Group's credit exposure, which is the maximum potential exposure including committed facilities:

	2012 €m	2011 €m
Non-derivative financial assets		
Loans and advances to customers	6,427	7,176
Loans and advances to credit institutions	128	130
Derivative financial instruments	35	56

Maximum exposure to credit risk – fair value of collateral

The following table presents the fair value of collateral held by the Bank for loans and advances to customers detailed in the maximum exposure to credit risk. The fair value of the collateral is capped at the loan outstanding amount.

The following table shows the fair value of collateral held for loans and advances to customers at end 2012 and 2011.

Collateral Held: Loans and advances to customers *

	2012 €m	2011 €m
Impaired loans	801	757
Past due but not impaired	429	421
Non impaired/non past due	4,462	5,238
Total loans	**5,692**	**6,416**

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Residential mortgages *

The Bank does not originate lending in its own right, but originates loans on a wholesale basis periodically from EBS. While EBS considers a borrower's repayment capacity to be paramount in granting any loan, EBS also takes collateral in support of lending transactions for the purchase of residential property. There are clear policies in place which set out the type of property which is acceptable as collateral and the loan to property value relationship. Collateral valuations are required at time of origination of each residential mortgage. The fair value at December 2012 of residential mortgages is based on the property values at origination and applying the CSO (Ireland) index to these values to take account of price movements in the interim. The collateral values above include all loans regardless of balance outstanding. Additional information in relation to LTV and Days Past Due profiles for residential mortgages is noted within the Risk Management Report.

Provisioning for impairment *

The accounting policies of loans and advances to customers are outlined in accounting policies. A loan or portfolio of loans is impaired and an impairment loss is incurred if there is objective evidence of impairment as a result of one or more loss events that occurred after the initial recognition of an asset or group of assets.

Objective evidence can include both:

- Micro conditions – for example a breach in the repayment contract, i.e. arrears on the account, and
- Macro conditions – for example an adverse change in economic conditions.

An impairment loss event is an event which has an impact on the expected cash flows of the asset. Where the event has been incurred and has been identified, an individual provision is required. Where the loss has been incurred but has not yet been identified, a collective provision is required.

Provisions are calculated for assets which are deemed to be impaired where there is objective evidence of impairment. If the asset is deemed to be significant, then it is reviewed on an individual basis. Where the asset is impaired, but not significant, it is reviewed on a pooled or collective basis. Provisions are also calculated on a pool basis for individual assets where there is no objective evidence of individual impairment yet, under the incurred but not reported ("INBR") assessment. In this way, all assets are reviewed.

For Residential Loan Assets, the Bank assess loans for impairment where; loans which are €0.01 or more in arrears and where the arrears is not of a technical nature, or where there is other evidence of impairment, for example, where an issue may arise in relation to a loan or group of loans such as a legal claim etc. Categories of loans that will be classed as impaired regardless of arrears include: loans where the property is in possession of EBS and loans where fraudulent activity is suspected.

Significant assets in the Bank are defined as assets with an overall current value of more than €1.5m. This applies to non-retail loan and treasury assets: the threshold for Retail assets is set at €0.75m. Assets which are impaired and which are significant are reviewed on an individual case basis.

The loan value threshold is not applied to loans

- where the property is in possession of the Bank; or
- where fraudulent activity is suspected or proven.

All such loans are also assessed individually for provision.

All loans greater than 90 days past due are deemed impaired, regardless of significance.

Collective Provisions *

All loans where the individual provision is zero, whether or not an individual assessment is completed, are part of the collective provision calculation.

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The calculation has three key components reflecting the three stages in the movement of a loan to loss: probability of default (PD); probability of repossession given default (PRGD); and loss given repossession (LGR).

Default is defined to be 3 (monthly) payments or more in arrears, i.e., at least 90 days past due. If a loan is already in default then its PD is 1, otherwise it is a number between 0 and 1 measuring the likelihood of the loan moving into default in the coming 12 months. The rate of default is adjusted to take into account expected movements in external macroeconomic factors (such as employment and GDP).

The rate of movement from default to repossession is assessed according to the number of payments missed – the deeper in default a loan is, the more likely it is that loss will result.

The calculation of incurred loss is driven largely by expectation of property values at disposal.

In this note, impaired assets are those for which an individual provision has been made.

Impairment Sensitivities 2012
Altering the key assumptions for provisions has varying impacts on the overall provision numbers. The following table shows the relative impacts of standardised changes.

Factor	
1. Probability of Default: Interest Rate changes	- A 1% increase in Standard Variable Rate leads to a 0.5% increase in collective provisions for Homeloans.
2. Probability of Default: Macroeconomic factors	- A 2% fall in employment leads to a 0.8% increase in collective provisions for Retail assets (Homeloans and Buy-to-Lets) - The GDP and GNP numbers alone have little influence.
3. Roll rate from repossession to loss: Higher roll rates assumed	An increase in 4% of the repossession rate will result in a 7.3% movement in stock of provisions.
4. Loss Given repossession: Higher reductions in house prices from peak	- An increased peak to trough assumption (changing to 58% from 55%) increases collective provisions by 9.2%.

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Impairment Sensitivities 2011	
Factor	
1. Probability of Default: Interest Rate changes	- A 1% increase in Standard Variable Rate leads to a 2.5% increase in collective provisions for Homeloans.
2. Probability of Default: Macroeconomic factors	- A 2% fall in employment leads to a 4.3% increase in collective provisions for Retail assets (Homeloans and Buy-to-Lets) - The GDP and GNP numbers alone have little influence.
3. Roll rate from repossession to loss: Higher roll rates assumed	- An increase in 5% of the repossession rate will result in a 10.6% movement in stock of provisions.
4. Loss Given repossession: Higher reductions in house prices from peak	- An increased peak to trough assumption (changing to 58% from 55%) increases collective provisions by 6.4%.

4. Credit Profile *

The analysis below in relation to residential loans for the Bank is based on gross lending before unearned income and impairment provisions of €249m (2011: €172m).

Credit quality *
The following table includes the Bank's loans and advances to customers gross of impairment provisions split on a core/non-core basis. Core includes home loans and non core includes buy to let loans.

Loans and advances to customers	2012 Core €m	2012 Non-core €m	2012 Total €m	2011 Core €m	2011 Non-core €m	2011 Total €m
Residential mortgages	6,660	16	6,676	6,949	399	7,348

Asset quality has been affected by an increase in the level of arrears, with 84.3% of the combined loan book maintaining a satisfactory payment profile in 2012 compared with 86.9% for 2011. The change in loan quality is reflected in a higher level of provisions, detailed below.

Impairment provisions	2012 Core €m	2012 Non-core €m	2012 Total €m	2011 Core €m	2011 Non-core €m	2011 Total €m
Statement of financial position provisions	246	3	249	147	25	172
Statement of financial position provisions as a % of loans and advances	3.7%	18.8%	3.7%	2.1%	6.3%	2.3%
Specific provision as a % of impaired loans	19.3%	33.3%	19.5%	16.3%	25.2%	17.2%
Impairment charge as a % of total loans	1.5%	37.5%	1.5%	1.6%	4.5%	1.8%

The Bank's loans and advances to customers amounted to €6,676m at 31 December 2012 and have decreased by €672m since December 2011. 27.2% or €1,817m (2011: 24.3% or €1,787m) of total Bank

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loans and advances to customers are criticised of which €1,051m or 15.7% (2011: €959m or 13.1%) is impaired.

Statement of financial position impairment provisions of €249m (2011: €172m) provide cover on impaired loans of 23.7% (2011: 17.9%) and on total loans of 3.7% (2011: 2.3%).

The income statement provision charge (including the unearned interest provision of €5m (2011: €1m)) in 2012 was €100m or 1.5% of total loans. The charge is down from €130m or 1.8% of total loans in 2011.

Residential mortgages *

Residential mortgages amounted to €6,676m at 31 December 2012. This compares to €7,348m at 31 December 2011, the decrease driven primarily by a deleveraging of €378m of BTL assets from the Bank in quarter 3 2012 and by repayments and redemptions during 2012.

The split of the residential mortgage book is owner-occupier, €6,660m and buy-to-let, €16m. The income statement impairment provision charge for 2012 was €94m or 1.4% for Residential mortgages. The statement of financial position impairment provisions (including unearned income provision) of €249m is held at 31 December 2012, split €205m specific and €44m collective.

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Residential mortgage – Total	2012			2011		
	Owner-occupier (Core) €m	Buy-to-let (Non-Core) €m	Total €m	Owner-occupier (Core) €m	Buy-to-let (Non-Core) €m	Total €m
Total residential mortgages	6,660	16	6,676	6,949	399	7,348
Arrears						
1 - 30 DPD* but not impaired	312	-	312	367	11	378
31 - 60 DPD but not impaired	118	-	118	84	5	89
61 - 90 DPD but not impaired	65	-	65	26	2	28
91 - 180 DPD but not impaired	23	-	23	-	-	-
Impaired Loans	1,042	9	1,051	865	94	959
of which impaired and not in arrears	107	1	108	80	8	88
of which impaired and in arrears	935	8	943	785	86	871
- of which 1 - 30 DPD	33	-	33	19	6	25
- of which 31 - 60 DPD	29	-	29	65	10	75
- of which 61 - 90 DPD	33	-	33	93	8	101
- of which 91 - 180 DPD	177	1	178	204	24	228
- of which 181 - 365 DPD	252	3	255	226	25	251
- of which over 365 DPD	411	4	415	177	13	190
Total Arrears (30+ DPD and/or impaired)	1,248	9	1,257	975	101	1,076
90+ DPD Arrears (90+ DPD and/or impaired)	1,065	9	1,074	865	94	959
Provisioning						
Statement of financial position specific provisions	202	3	205	142	24	166
Statement of financial position IBNR provisions	44	-	44	4	2	6
Income statement specific provisions YTD	56	1	57	14	2	16
Income statement specific IBNR provisions YTD	38	5	43	97	15	112
Specific provisions / impaired loans cover			19.5%			17.2%

* = DPD is Days past due

The portfolio has experienced an increase in arrears reflecting the impact of a harsher economic climate on borrowers' repayment affordability. The level of loans >90 days in arrears or impaired was 16.1% at 31 December 2012 compared with 13.4% at 31 December 2011.

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The level of loans >90 days in arrears or impaired in the owner occupier book has increased significantly since 31 December 2011 from €891m (12.8% of mortgages) to €1,065m or 16.0% at 31 December 2012. Unemployment, wage cuts and high levels of personal debt continued to be the principal drivers of increased arrears.

The level of loans >90 days in arrears or impaired in the Buy-to-Let ('BTL') portfolio has decreased significantly from €96m (24.1% at 31 December 2011) to €9m (56.3% at 31 December 2012). This change is due the deleveraging of buy to let assets in 2012 (approx. €378m) but a high percentage of accounts >90 days in arrears or impaired persists.

Total owner occupier and BTL loans >90 days past due or impaired amounted to €1,074m at 31 December 2012. Total specific provisions of €205m provided cover of 19.4% of impaired loans and have been raised due to the continued increase in >90 days past due or impaired loan balance. Statement of financial position collective provisions of €44m are held for the performing book (0.1% of the performing residential mortgage book) based on management's view of incurred loss in this book. The total income statement charge for 2012 was €100m (specific €57m and collective €43m).

EBS has received a number of requests for forbearance from customers who are experiencing cash flow difficulties. EBS considers these against the borrowers' current and likely future financial circumstances, their willingness to resolve these issues, as well as the legal and regulatory obligations. As part of that process loans are tested for impairment and where appropriate, the loans are downgraded to impaired status and provisions raised.

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4.1 Asset Quality *

The following tables show criticised loans for the total loan book split into Core and Non-Core assets. Criticised loans include watch, vulnerable and impaired loans.

Asset quality – Residential Mortgages	2012				2011			
	Core €m	Non-core €m	Total €m	%	Core €m	Non-core €m	Total €m	%
Satisfactory	**4,854**	**5**	**4,859**	**72.8**	**5,314**	**247**	**5,561**	**75.7**
Watch	542	1	543	**8.1**	624	48	672	9.1
Vulnerable	222	1	223	**3.4**	145	10	155	2.1
Impaired	1,042	9	1,051	**15.7**	866	94	960	13.1
Criticised	**1,806**	**11**	**1,817**	**27.2**	**1,635**	**152**	**1,787**	**24.3**
Gross loans	**6,660**	**16**	**6,676**	**100.0**	**6,949**	**399**	**7,348**	**100.0**
Criticised as a % of total gross loans	27.1%	68.8%	27.2%		23.5%	38.1%	24.3%	
Impaired as % of total gross loans	15.6%	56.3%	15.7%		12.5%	23.6%	13.1%	

The Bank's criticised loans and advances to customers amounted to €1,817m or 27.2% of total customer loans. The Bank's criticised loans have increased by €30m since 31 December 2011, with an increase of €171m in the owner-occupier portfolio being offset by the deleverage of buy-to-let assets. The main drivers of the increases in criticised loans has been the impact of the continuing lack of activity in the property sector and consequent impact on the housing sector, together with high levels of unemployment and reduced earnings which negatively affected borrowers' ability to repay loans.

Total impaired loans	2012 €m	2012 %	2011 €m	2011 %
Impaired loans – Core	1,042	15.6	865	11.8
Impaired loans – Non Core	9	0.1	94	1.3
Total	**1,051**	**15.7**	**959**	**13.1**

The Bank's impaired loans are up €91m in the year to €1,051m (or 15.7% of total loans) mainly in the residential mortgage portfolio. This is mainly due to the underlying deterioration in the book.

Past due but not impaired

Balances due on core loans categorised as past due but not impaired increased by €40m in 2012 compared with 2011 as concerns regarding repayments became evident.

	2012				2011			
	Core €m	Non-core €m	Total €m	%	Core €m	Non-core €m	Total €m	%
Neither past due nor impaired	5,099	7	5,106	76.4	5,606	287	5,893	80.2
Past due but not impaired	518	-	518	7.8	478	18	496	6.7
Impaired – no provision	46	1	47	0.7	26	10	36	0.5
Impaired –provision held	997	8	1,005	15.1	839	84	923	12.6
Gross loans and advances	**6,660**	**16**	**6,676**	**100.0**	**6,949**	**399**	**7,348**	**100.0**
Provision for impairment	246	3	249		147	25	172	
Total loans and advances after provisions	**6,414**	**13**	**6,427**		**6,802**	**374**	**7,176**	**100.0**

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Loans neither past due nor impaired have decreased from 80.2% of loan balances in 2011 to 76.4% as at December 2012. The value of loans past due has increased from 19.8% in 2011 to 23.6% in 2012.

Aged analysis of loans and advances which are past due but not impaired
Residential loans up to 90 days past due are not categorised as impaired. Non-core loans are assessed on a case by case basis.

	2012				2011			
	Core	Non-core	Total	%	Core	Non-core	Total	%
	€m	€m	€m		€m	€m	€m	
1 – 30 days	312	-	312	60.1	367	11	378	76.3
31 – 60 days	118	-	118	22.8	84	5	89	17.9
61 – 90 days	65	-	65	12.6	26	2	28	5.8
91 – 180 days	23	-	23	4.5	-	-	-	-
Total	518	-	518	**100**	477	**18**	**495**	**100.0**

Provisions are calculated for assets which are deemed to be impaired where there is objective evidence of impairment. If the asset is deemed to be significant, then it is reviewed on an individual basis. Where the asset is impaired, but not significant, it is reviewed on a collective basis.

2012	Loans & Advances	Impaired Loans & Advances	Impaired % of Loans	Individually Assessed	Collectively Assessed	Total Impairment Provision	Provision as % of impaired loans
Residential	6,676	1,051	15.7%	205	44	249	23.8%
Total	6,676	1,051	15.7%	205	44	249	23.8%

2011	Loans & Advances	Impaired Loans & Advances	Impaired % of Loans	Individually Assessed	Collectively Assessed	Total Impairment Provision	Provision as % of impaired loans
Residential	7,348	960	13.1%	166	6	172	17.9%
Total	**7,348**	**960**	**13.1%**	**166**	**6**	**172**	**17.9%**

Global and domestic economic markets continued to experience difficulties throughout 2012 which impacted negatively on the Group's lending portfolios.

The Bank's income statement provision charge for loans and advances to customers was €100m or 1.5% of loan balances and included a specific provision charge of €57m and a collective provision charge of €43m. 94.3% of the charge related to owner-occupier residential mortgages with the remainder 5.7% for borrowers in the buy-to-let sector.

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4.2 Forbearance

The incidence of the main type of forbearance arrangements for residential mortgages is analysed below.

			2012*	
Owner Occupier Mortgages	**Total loans in forbearance**		**Loans >90 days in arrears and/or impaired at period end**	
	Number of loans	**Balance €m**	**Number of loans**	**Balance €m**
TEMPORARY RESTRUCTURES				
Interest Only	2,684	424	833	146
Deferred Interest Scheme	3	1	1	-
Other	168	21	76	10
Temporary Restructures Sub-total	**2,855**	**446**	**910**	**156**
PERMANENT RESTRUCTURES				
Arrears capitalisation	634	93	400	57
Term extension	1,948	166	271	22
Split mortgage	2	0	1	-
Permanent Restructures Sub-total	**2,584**	**259**	**672**	**79**
Total	**5,439**	**705**	**1,582**	**235**

				2012*
Buy-to-let Mortgages	**Total loans in forbearance**		**Loans >90 days in arrears and/or impaired at period end**	
	Number of loans	**Balance €m**	**Number of loans**	**Balance €m**
TEMPORARY RESTRUCTURES				
Interest Only	13	2	8	2
Other	1	-	-	-
Temporary Restructures Sub-total	14	2	8	2
PERMANENT RESTRUCTURES				
Arrears capitalisation	-	-	-	-
Term extension	7	1	-	-
Permanent Restructures Sub-total	7	1	-	-
Total	21	3	8	2

**Forms integral part of the audited financial statements*

Total Mortgages	Total loans in forbearance		Loans >90 days in arrears and/or impaired at period end	
				2012*
	Number of loans	Balance €m	Number of loans	Balance €m
TEMPORARY RESTRUCTURES				
Interest Only	2,697	426	841	148
Deferred Interest Scheme	3	1	1	-
Other	169	21	76	10
Temporary Restructures Sub-total	2,869	448	918	158
PERMANENT RESTRUCTURES				
Arrears capitalisation	634	93	400	57
Term extension	1,955	167	271	22
Split mortgage	2	-	1	-
Permanent Restructures Sub-total	2,591	260	672	79
Total	5,460	708	1,590	237

Owner Occupier Mortgages	Total loans in forbearance		Loans >90 days in arrears and/or impaired at period end	
				2011
	Number of loans	Balance €m	Number of loans	Balance €m
TEMPORARY RESTRUCTURES				
Interest Only	2,548	430	718	120
Deferred Interest Scheme	1	-	-	-
Other	103	13	47	5
Temporary Restructures Sub-total	2,652	443	765	125
PERMANENT RESTRUCTURES				
Arrears capitalisation	340	52	-	-
Term extension	1,934	168	210	16
Permanent Restructures Sub-total	2,274	220	210	16
Total	4,926	663	975	141

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Buy-to-let Mortgages	Total loans in forbearance		2011 Loans >90 days in arrears and/or impaired at period end	
	Number of loans	Balance €m	Number of loans	Balance €m
TEMPORARY RESTRUCTURES				
Interest Only	283	58	87	18
Other	4	1	2	1
Temporary Restructures Sub-total	287	59	89	19
PERMANENT RESTRUCTURES				
Arrears capitalisation	-	-	-	-
Term extension	103	17	6	1
Permanent Restructures Sub-total	103	17	6	1
Total	390	76	95	20

Total Mortgages	Total loans in forbearance		2011 Loans >90 days in arrears and/or impaired at period end	
	Number of loans	Balance €m	Number of loans	Balance €m
TEMPORARY RESTRUCTURES				
Interest Only	2,831	488	805	138
Deferred Interest Scheme	1	-	-	-
Other	107	14	49	6
Temporary Restructures Sub-total	2,939	502	854	144
PERMANENT RESTRUCTURES				
Arrears capitalisation	340	52	-	-
Term extension	2,037	185	216	17
Permanent Restructures Sub-total	2,377	237	216	17
Total	5,316	739	1,074	161

The types of forbearance measures that are currently considered for mortgage customers are interest only, arrears capitalisation, term extension and deferred interest scheme. EBS has developed a Mortgage Arrears Resolution Strategy ("MARS") for dealing with customers in difficulty or likely to be in difficulty. Of the total residential mortgage book of €708m, 10.6% are subject to forbearance measures as at 31 December 2012, compared to 9.7% as at 31 December 2011. €237m (33.4%) of the loans under forbearance were >90 days past due or impaired as at 31 December 2012, compared to 24.5% as at 31 December 2011.

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Analysis by Loan-to-value ('LTV') of Residential Mortgage Lending

			2012*
Forbearance stock	**Owner Occupier**	**BTL**	**Total**
	€m	**€m**	**€m**
Less than 50%	52	-	52
50% - 70%	65	1	66
71% - 80%	45	-	45
81% - 90%	50	-	50
91% - 100%	55	-	55
101% - 120%	107	-	107
121% - 150%	164	1	165
Greater than 150%	167	1	168
Total	705	3	708

			2011
Forbearance stock	**Owner Occupier**	**BTL**	**Total**
	€m	**€m**	**€m**
Less than 50%	53	2	55
50% - 70%	71	3	74
71% - 80%	46	4	50
81% - 90%	51	5	56
91% - 100%	59	7	66
101% - 120%	115	18	133
121% - 150%	154	26	180
Greater than 150%	114	11	125
Total	663	76	739

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Credit profile of Residential Mortgages in Forbearance

Past due but not impaired

Forbearance stock	31 December 2012*			31 December 2011		
	Owner Occupier	Buy-to-let	Total	Owner Occupier	Buy-to-let	Total
	€m	€m	€m	€m	€m	€m
0 - 30 days	57	-	57	70	2	72
31 - 60 days	31	-	31	26	2	28
61 - 90 days	13	-	13	10	-	10
91 - 180 days	7	-	7	-	-	-
181 - 365 days	-	-	-	-	-	-
Over 365 days	-		-	-	-	-
Total past due but not impaired	108	-	108	106	4	110

Forbearance stock – Impaired

Forbearance stock	31 December 2012*			31 December 2011		
	Owner Occupier	Buy-to-let	Total	Owner Occupier	Buy-to-let	Total
	€m	€m	€m	€m	€m	€m
Not Past Due	42	-	42	20	2	22
0 - 30 days	17	-	17	5	2	7
31 - 60 days	12	-	12	17	4	21
61 - 90 days	8	-	8	27	4	31
91 - 180 days	49	1	50	49	4	53
181 - 365 days	53	1	54	31	3	34
Over 365 days	48	-	48	9	1	10
Total past due but not impaired	229	2	231	158	20	178

Summary	**31 December 2012***			**31 December 2011**		
Past due but not impaired	108	-	108	106	4	110
Impaired	229	2	231	158	20	178
Neither past due nor impaired	368	2	370	400	51	451
Total forbearance stock	705	3	708	663	76	739

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4.3 Residential Repossessions*

The Bank held 11 properties at year end, representing a decrease of 4 compared with 2011 year end. The Bank disposed of 10 repossessed properties in 2012.

Residential Mortgages - Repossessions **2012**

Movements in residential repossessions	Owner occupier		Buy to let		Total	
	No. of properties	Loan balance at repossession €m	No. of properties	Loan balance at repossession €m	No. of properties	Loan balance at repossession €m
Opening stock 1 January 2012	15	4	-	-	15	4
Repossessions in 2012	6	2	4	1	10	3
Disposals	(8)	(2)	-	-	(8)	(2)
Closing stock 31 Dec 2012	13	4	4	1	17	5
Of which at 31 Dec 2012:						
Voluntary Surrenders	4	-	4	-	8	-
Enforcement of security	2	-	-	-	2	-
	6	-	**4**	-	**10**	-

Residential Mortgages - Repossessions **2011**

Movements in residential repossessions	Owner occupier		Buy to let		Total	
	No. of properties	Loan balance at repossession €m	No. of properties	Loan balance at repossession €m	No. of properties	Loan balance at repossession €m
Opening stock 1 January 2011	6	2	-	-	6	2
Repossessions in 2011	9	2	-	-	9	2
Disposals	-	-	-	-	-	-
Closing stock 31 Dec 2011	15	4	-	-	15	4
Of which at 31 Dec 2011:	8	-	-	-	8	-
Voluntary Surrenders	1	-	-	-	1	-
Enforcement of security	-	-	-	-	-	-
	9	-	-	-	9	-

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Stock/Activity	Number of repossessions	Balance	Gross sales proceeds	Cost to sell	Loss on sale	Weighted Average LTV at sale
		€m	€m	€m	€m	%
2012						
Owner Occupier	8	2	1	-	2	353%
Buy-to-let	-	-	-	-	-	-
Total repossessions	**8**	**2**	**1**	**-**	**2**	**353%**
2011						
Owner Occupier	15	4	-	-	-	-
Buy-to-let	-	-	-	-	-	-
Total repossessions	**15**	**4**	**-**	**-**	**-**	**-**

4.4 Residential mortgage lending - index linked LTV

Residential mortgage lending - Total

The property values used in the completion of the following loan to value ("LTV") tables are determined with reference to the most recent valuation indexed to the Central Statistics Office ("CSO") Residential Property Price Index.

2012*	Owner Occupier	BTL	Total
	€m	€m	€m
Less than 50%	718	1	719
50% - 70%	682	1	683
71% - 80%	404	-	404
81% - 90%	439	1	440
91% - 100%	471	-	471
101% - 120%	1,145	2	1,147
121% - 150%	1,377	6	1,383
Greater than 150%	1,424	5	1,429
Total	**6,660**	**16**	**6,676**

2011	Owner Occupier	BTL	Total
	€m	€m	€m
Less than 50%	832	27	859
50% - 70%	783	23	806
71% - 80%	462	18	480
81% - 90%	510	18	528
91% - 100%	528	23	551
101% - 120%	1,297	90	1,387
121% - 150%	1,409	143	1,552
Greater than 150%	1,128	57	1,185
Total	**6,949**	**399**	**7,348**

40.7% of the owner-occupier and 21.9% of the buy-to-let mortgages (by exposure) were in positive equity at 31 December 2012. In terms of the total portfolio, 59.3% was in negative equity at 31 December 2012, reflecting the continuing decline in residential property prices in Ireland in 2012. The

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weighted average indexed loan to value ratio for the total book was 111% as at 31 December 2012 whilst the indexed loan to value ratio for the >90 days past due or impaired book was higher at 133%.

Residential - Neither past due nor impaired

The following tables profile the residential mortgage portfolio that is neither past due nor impaired by the indexed loan to value ratios at 31 December 2012 and 2011.

2012*	Owner Occupier €m	BTL €m	Total €m
Less than 50%	627	1	628
50% - 70%	568	-	568
71% - 80%	333	-	333
81% - 90%	366	-	366
91% - 100%	379	1	380
101% - 120%	935	1	936
121% - 150%	1,018	2	1,020
Greater than 150%	873	2	875
Total	**5,099**	**7**	**5,106**

2011	Owner Occupier €m	BTL €m	Total €m
Less than 50%	746	23	769
50% - 70%	672	18	690
71% - 80%	399	14	413
81% - 90%	433	15	448
91% - 100%	435	17	452
101% - 120%	1,089	67	1,156
121% - 150%	1,074	97	1,171
Greater than 150%	758	36	794
Total	**5,606**	**287**	**5,893**

Among loans neither past due nor impaired, 44.6% of the owner-occupier and 28.6% of the buy-to-let mortgages were in positive equity at 31 December 2012. In terms of the total portfolio, 55.4% was in negative equity at 31 December 2012, reflecting the continuing decline in residential property prices in Ireland in 2012

90 days past due or impaired

LTV ratio of residential mortgage lending (index linked) which are 90 days past due.

The following tables profiles the residential mortgage portfolio that was > 90 days past due and /or impaired by the indexed loan to value ratios at 31 December 2012 and 2011

2012*	Owner Occupier €m	BTL €m	Total €m
Less than 50%	54	-	54
50% - 70%	74	-	74
71% - 80%	44	1	45
81% - 90%	41	1	42
91% - 100%	59	-	59
101% - 120%	126	1	127
121% - 150%	237	3	240
Greater than 150%	430	3	433
Total	**1,065**	**9**	**1,074**

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2011	Owner Occupier €m	BTL €m	Total €m
Less than 50%	44	3	47
50% - 70%	63	4	67
71% - 80%	36	3	39
81% - 90%	46	3	49
91% - 100%	54	4	58
101% - 120%	126	20	146
121% - 150%	219	39	258
Greater than 150%	277	18	295
Total	**865**	**94**	**959**

25.6% of the owner-occupier and 12.5% of the buy-to-let mortgages were in positive equity at 31 December 2012. In terms of the total portfolio, 74.5% was in negative equity at 31 December 2012, reflecting the continuing decline in residential property prices in Ireland in 2012.

Residential Mortgage lending with Fair Value Collateral

Residential mortgage lending - Total

The property values used in the completion of the following loan to value ("LTV") tables are determined with reference to the most recent valuation indexed to the Central Statistics Office ("CSO") Residential Property Price Index.

2012*	Owner Occupier €m	BTL €m	Total €m
Fully Collateralised			
Less than 50%	718	1	719
50% - 70%	682	1	683
71% - 80%	404	1	404
81% - 90%	439	1	440
91% - 100%	471	-	471
Partially Collateralised			
Book Value	3,946	13	3,959
Value of Collateral	*2,966*	*9*	2,975
Total	**6,660**	**16**	**6,676**

2011	Owner Occupier €m	BTL €m	Total €m
Fully Collateralised			
Less than 50%	832	27	859
50% - 70%	783	22	805
71% - 80%	462	18	480
81% - 90%	510	18	528
91% - 100%	528	23	551
Partially Collateralised			
Book Value	3,834	291	4,125
Value of Collateral	*2,969*	*224*	*3,193*
Total	**6,949**	**399**	**7,348**

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Residential - Neither Past Due nor Impaired

The following tables profile the residential mortgage portfolio that is neither past due nor impaired by the indexed loan to value ratio's at 31 December 2012 and 2011.

2012*	Owner Occupier €m	BTL €m	Total €m
Fully Collateralised			
Less than 50%	627	1	628
50% - 70%	568	-	568
71% - 80%	333	-	333
81% - 90%	366	-	367
91% - 100%	379	-	380
Partially Collateralised			
Book Value	2,825	4	2,829
Value of Collateral	*2,182*	*3*	2,185
Total	**5,099**	**7**	**5,106**

2011	Owner Occupier €m	BTL €m	Total €m
Fully Collateralised			
Less than 50%	746	23	769
50% - 70%	672	18	690
71% - 80%	399	14	413
81% - 90%	433	15	448
91% - 100%	435	17	452
Partially Collateralised			
Book Value	2,921	200	3,121
Value of Collateral	*2,311*	*155*	*2,466*
Total	**5,606**	**287**	**5,893**

*Forms integral part of the audited financial statements

Residential – Past due not impaired

The following tables profile the residential mortgage portfolio that is past due not impaired by the indexed loan to value ratio's at 31 December 2012 and 2011.

2012*	Owner Occupier €m	BTL €m	Total €m
Fully Collateralised			
Less than 50%	38	-	38
50% - 70%	42	-	42
71% - 80%	27	-	27
81% - 90%	32	-	32
91% - 100%	33	-	33
Partially Collateralised			
Book Value	346	-	346
Value of Collateral	*257*	-	257
Total	**518**	**-**	**518**

Residential – Past due not impaired

2011	Owner Occupier €m	BTL €m	Total €m
Fully Collateralised			
Less than 50%	42	1	43
50% - 70%	47	1	48
71% - 80%	27	1	28
81% - 90%	31	1	32
91% - 100%	39	-	39
Partially Collateralised			
Book Value	291	14	305
Value of Collateral	219	11	230
Total	**477**	**18**	**495**

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Residential – 90 Days past due and / or impaired

LTV ratio of residential mortgage lending (index linked) which are 90 days past due. The following tables profiles the residential mortgage portfolio that was > 90 days past due and /or impaired by the indexed loan to value ratios at 31 December 2012 and 2011

2012*	Owner Occupier €m	BTL €m	Total €m
Fully Collateralised	54	-	54
Less than 50%	75	-	75
50% - 70%	44	1	45
71% - 80%	41	1	42
81% - 90%	59	-	59
91% - 100%			
Partially Collateralised			
Book Value	792	7	799
Value of Collateral	540	5	545
Total	**1,065**	**9**	**1,074**

2011	Owner Occupier €m	BTL €m	Total €m
Fully Collateralised			
Less than 50%	44	3	47
50% - 70%	63	4	67
71% - 80%	37	3	40
81% - 90%	45	3	48
91% - 100%	54	4	58
Partially Collateralised			
Book Value	622	77	699
Value of Collateral	439	58	497
Total	**865**	**94**	**959**

Residential – Impaired

LTV ratio of residential mortgage lending (index linked) which is impaired. The following tables profiles the residential mortgage portfolio that was impaired by the indexed loan to value ratios at 31 December 2012 and 2011.

2012*	Owner Occupier €m	BTL €m	Total €m
Fully Collateralised			
Less than 50%	52	-	52
50% - 70%	73	-	73
71% - 80%	44	-	44
81% - 90%	40	1	41
91% - 100%	59	-	59
Partially Collateralised			
Book Value	774	8	782
Value of Collateral	527	5	532
Total	**1,042**	**9**	**1,051**

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2011	Owner Occupier €m	BTL €m	Total €m
Fully Collateralised			
Less than 50%	44	3	47
50% - 70%	63	4	67
71% - 80%	37	3	40
81% - 90%	45	3	48
91% - 100%	54	4	58
Partially Collateralised			
Book Value	622	77	699
Value of Collateral	439	58	497
Total	**865**	**94**	**959**

Vintage analysis – Residential and Impaired

The following table profiles the Republic of Ireland residential mortgage book and impaired residential mortgage book at 31 December 2012 and 2011 by year of origination.

2012*	Residential Mortgage Loan Book		Loans >90 days in arrears but not impaired at period end		Loans classified as impaired at period end		Loans >90 days in arrears and/or impaired at period end	
Total	Number of loans	Balance €m	Number of loans	Balance €m	Number of loans	Balance €m	Number of loans	Balance €m
1996 and before	4,297	114	6	-	328	16	334	16
1997	1,103	36	1	-	87	4	88	4
1998	1,220	44	4	-	97	5	101	5
1999	1,391	60	1	-	129	10	130	10
2000	1,557	94	4	-	137	11	141	11
2001	1,912	148	4	-	166	15	170	15
2002	2,657	240	5	-	221	23	226	23
2003	3,091	261	10	1	329	32	339	33
2004	3,479	334	14	2	376	45	390	47
2005	5,098	533	13	2	590	88	603	90
2006	8,231	1,214	25	4	1,136	220	1,161	224
2007	7,675	1,223	32	5	1,507	288	1,539	293
2008	7,364	1,079	32	5	1,361	230	1,393	235
2009	4,798	609	14	2	394	48	408	50
2010	4,677	632	14	2	124	16	138	18
2011	437	55	-	-	2	-	2	-
2012	1	-	-	-	-	-	-	-
Total	58,988	6,676	179	23	6,984	1,051	7,163	1,074

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2011 Total	Residential Mortgage Loan Book Number of loans	Balance €m	Loans >90 days in arrears but not impaired at period end Number of loans	Balance €m	Loans classified as impaired at period end Number of loans	Balance €m	Loans >90 days in arrears and/or impaired at period end Number of loans	Balance €m
1996 and before	5,094	140	-	-	291	14	291	14
1997	1,310	44	-	-	81	4	81	4
1998	1,396	53	-	-	88	5	88	5
1999	1,557	70	-	-	114	8	114	8
2000	1,687	107	-	-	113	9	113	9
2001	2,056	163	-	-	143	13	143	13
2002	3,109	282	-	-	211	22	211	22
2003	3,309	291	-	-	276	28	276	28
2004	3,793	385	-	-	336	42	336	42
2005	5,777	638	-	-	575	96	575	96
2006	8,945	1,362	-	-	1,031	205	1,031	205
2007	8,293	1,327	-	-	1,360	264	1,360	264
2008	7,748	1,158	-	-	1,184	203	1,184	203
2009	4,989	629	-	-	307	37	307	37
2010	4,773	643	-	-	73	10	73	10
2011	442	56	-	-	-	-	-	-
Total	64,278	7,348	-	-	6,183	959	6,183	959

4.5 Analysis of loans and advances to customers by contractual residual maturity and interest rate sensitivity *

The following tables analyse gross loans to customers by maturity and interest rate sensitivity. Approximately 16% of Bank's mortgage portfolio is provided on a fixed rate basis. The interest rate risk exposure is managed by AIB Group Treasury within agreed policy parameters.

Loans and advances to customers

	Fixed €m	Variable €m	Total €m	Within 1 year €m	After 1 year but within 5 years €m	After 5 years €m	Total €m
2012	1,038	5,638	6,676	1,072	93	5,511	6,676
2011	1,582	5,766	7,348	679	109	6,560	7,348

4.6 Cross-border outstandings *

Cross-border outstandings are based on the country of domicile of the borrower and comprise placings with banks and money at call and short notice, loans to customers (including those held within discontinued operations), other monetary assets, including non-local currency claims of overseas offices on local residents. The Bank monitors geographic breakdown based on the country of the borrower and the guarantor of ultimate risk. There were no cross-border outstandings at 31 December 2012 (2011: Nil).

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4.7 Treasury assets and derivatives *

Treasury assets consist of cash and balances with central banks, derivative financial instruments, available-for-sale, and loans and advances to credit institutions excluding operating bank accounts.

The following tables present an analysis of Treasury asset counterparties based on the Bank's internal ratings mapped to an external rating agency scale. Where the counterparty is government guaranteed we have used the sovereign rating.

	Derivatives €m	Loans & Advances to Credit Institutions €m
2012		
Balances at 31 December 2012	35	128
Aaa	-	-
Aa3 to Aa1	-	-
A3 to A1	-	23.5%
Lower than A3	100%	76.5%
Unrated	-	-
2011		
Balances at 31 December 2011	56	130
Aaa	-	-
Aa3 to Aa1	3%	-
A3 to A1	-	87%
Lower than A3	97%	13%
Unrated	-	-

The Bank has established and enforces operating limits and other practices that maintain exposures within levels consistent with their internal policies. The Bank adheres to the principles of sound practices for managing interest rate risk and complies with any regulatory requirements as a minimum.

The Bank transacts derivatives for the purpose of reducing or eliminating Interest Rate Risk in the Banking Book (IRRBB). The Bank only uses interest rate swaps for this purpose. Treasury Assets are monitored on a daily basis.

Exposure to liquidity risk *

The following table analyses gross contractual maturities of financial liabilities including interest payable at the next interest payment date held by the Bank.

	Up to 1 month €m	Over 1 month to 3 months €m	Over 3 months to 6 months €m	Over 6 months to 1 year €m	1 to 2 years €m	Over 3 years €m	Total €m
31 December 2012							
Financial Liabilities							
Deposits by credit institutions	3,254	-	-	-	-	-	3,254
Derivative financial instruments	-	-	-	-	-	36	36
Debt securities in issue	1	4	-	400	700	2,050	3,155
	3,255	4	-	400	700	2,086	6,445

*Forms integral part of the audited financial statements

	Up to 1 month €m	Over 1 month to 3 months €m	Over 3 months to 6 months €m	Over 6 months to 1 year €m	1 to 2 years €m	Over 3 years €m	Total €m
31 December 2011							
Financial Liabilities							
Deposits by credit institutions	3,614	-	-	-	-	-	3,614
Derivative financial instruments	-	-	-	-	-	54	54
Debt securities in issue	5	-	-	1,039	650	1,950	3,644
	3,619	**-**	**-**	**1,039**	**650**	**2,004**	**7,312**

The previous tables show the undiscounted cash flows (other than for derivatives) on the Bank's financial liabilities on the basis of contractual maturity. Liabilities are included according to the earliest possible date of obligation. The disclosure for derivatives shows a net amount as the derivatives are all net settled. The Bank's expected cash flows on these instruments (other than derivatives) may vary significantly from this analysis. Liquidity is managed on a behavioural basis based on back tested historical performance and stress tested on an ongoing basis. For example, deposits by credit institutions are expected to maintain a stable or increasing balance.

Market risk*

Interest rate sensitivity gap analysis 2012

Interest rate risk is the risk that changes in interest rates will affect the Bank's income or the value of its holdings of financial instruments. The objective of interest rate risk management is to manage and control interest rate risk exposures within acceptable parameters, while optimising the return on risk.

The Bank has outsourced the measurement and reporting management of its interest rate risk to EBS. EBS Treasury measures and manages these risks using gap and sensitivity analysis. Derivatives such as interest rate swaps are used by the Bank for hedging purposes (reducing risk) only. The EBS Management team monitors these risks at an EBS level and are responsible for monitoring how interest rate risk are managed and ensuring that the Bank's policy is adhered to.

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Interest rate sensitivity gap analysis 2012 *

The tables below give an indication of the interest rate re-pricing mismatch in the Bank's statement of financial position. A cumulative net liability position in a time band indicates an exposure to a rise in interest rates.

	Not more than 3 months €m	Over 3 months but not more than 12 months €m	Over 1 year but not more than 5 years €m	Over 5 years €m	Non Interest Bearing €m	Trading €m	Total €m
2012							
Non-trading book							
Assets							
Loans and advances to credit institutions	128	-	-	-	-	-	128
Loans and advances to customers	6,047	393	208	28	(249)	-	6,427
Other assets	-	-	-	-	24	35	59
Total assets	**6,175**	**393**	**208**	**28**	**(225)**	**35**	**6,614**
Liabilities							
Debt securities in issue	2,969	-	-	-	-	-	2,969
Deposits by credit institutions	3,254	-	-	-	-	-	3,254
Other liabilities	-	-	-	-	2	36	38
Total shareholders' equity	-	-	-	-	353	-	353
Total liabilities	**6,223**	**-**	**-**	**-**	**355**	**36**	**6,614**
Interest rate sensitivity gap	**(48)**	**393**	**208**	**28**	**(580)**	**(1)**	**-**
Cumulative gap	**(48)**	**345**	**553**	**581**	**1**	**-**	**-**

Forms integral part of the audited financial statements

Interest rate sensitivity gap analysis 2011

	Not more than 3 months €m	Over 3 months but not more than 12 months €m	Over 1 year but not more than 5 years €m	Over 5 years €m	Non Interest Bearing €m	Trading €m	Total €m
2011							
Non-trading book							
Assets							
Loans and advances to credit institutions	130	-	-	-	-	-	130
Loans and advances to customers	5,831	436	1,027	53	(171)	-	7,176
Other assets	-	-	-	-	13	56	69
Total assets	**5,961**	**436**	**1,027**	**53**	**(158)**	**56**	**7,375**
Liabilities							
Debt securities in issue	2,269	999	-	-	-	-	3,268
Deposits by credit institutions	3,614	-	-	-	-	-	3,614
Other liabilities	-	-	-	-	8	54	62
Total shareholders' equity	-	-	-	-	431	-	431
Total liabilities	**5,883**	**999**	**-**	**-**	**439**	**54**	**7,375**
Derivatives	(1,000)	-	1,000	-	-	-	-
Interest rate sensitivity gap	**(922)**	**(563)**	**2,027**	**53**	**(597)**	2	-
Cumulative gap	**(922)**	**(1,485)**	**542**	**595**	**(2)**	-	-

In the tables above the assets and liabilities are allocated to time buckets based on the next re-pricing date of the individual assets and liabilities underlying the categories above.

There are some limitations associated with the above analysis, mainly due to market effects, over aggregation and run-offs. However, measures have been taken to minimise the effect of these limitations in line with industry practice and we are satisfied that the sensitivity analysis is an appropriate tool for measuring interest rate risk.

Interest rate stress testing *

EBS conducts daily stress testing on the Banking Book Portfolio, evaluating the exposure of the AIB Group and EBS to a parallel interest rate shift of 100 bps and a series of yield curve twist tests. The results of these stress tests are presented to the EBS Management team on a monthly basis. EBS is in the process of aligning such stress testing methodologies to those employed by AIB Group.

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The tables below provide an analysis of the Bank's sensitivity to an increase or decrease in market rates:

		100 bps parallel shift (increase/decrease) 2012 €m		2011 €m
Banking book portfolio				
Average for the period	- / +	1	- / +	1
Maximum for the period	- / +	3	- / +	3
Minimum for the period	- / +	-	- / +	-

The above table shows the present value effect that would be realised in the Income Statement on an accruals basis on the banking book and reserve investment book over the life of the assets and liabilities contained therein.

Overall interest rate risk positions are managed by EBS Treasury in conjunction with AIB Group Treasury.

Exposure to other market risks

Fair value risk *
The following table represents the fair value of financial instruments, including those not reflected in the financial statements at fair value. It is accompanied by a discussion of the methods used to determine fair value for financial instruments. In addition we have also set out the accounting classifications of each of the assets and liabilities. Where assets or liabilities are in a fair value hedge relationship the underlying asset or liability is also marked to market.

		2012			2011		
Assets	**Accounting classifications**	**Carrying value €m**	**Fair value €m**	**Unrecognised gain / (loss) €m**	**Carrying value €m**	**Fair value €m**	**Unrecognised gain / (loss) €m**
Derivative financial instruments	Fair value	35	35	-	56	56	-
Loans and advances to credit institutions	Loans and advances	128	128	-	130	130	-
Loans and advances to customers	Loans and advances	6,427	5,919	(508)	7,176	6,315	(861)
Liabilities							
Deposits by credit institutions	Amortised cost	3,254	3,254	-	3,614	3,614	-
Derivative financial instruments	Fair value	36	36	-	54	54	
Debt securities in issue	Amortised cost	2,969	2,788	(181)	3,268	2,912	(356)

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. For financial instruments carried at fair

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value, market prices or rates are used to determine fair value where an active market exists (for example a recognised stock exchange), which is the best evidence of the fair value of the financial instrument. For all financial assets held at fair value the Bank has applied Fair Value based upon quoted market prices where available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar instruments and adjusted for differences between the quoted instrument and the instrument being valued. In certain cases, including some loans and advances to customers, where there are no ready markets, various techniques have been used to estimate the fair value of the instruments.

Market prices are not available for all financial assets and liabilities held or issued by the Bank. Where no market price is available, fair values are estimated using valuation techniques. These are generally applied to over-the-counter (OTC) derivatives, unlisted trading assets and unlisted financial investments. The most frequently applied pricing models and valuation techniques include present value of future cash flows and option models. The valuations arrived at by applying these techniques are significantly affected by the choice of valuation model used and the underlying assumptions made concerning factors such as the amounts and timing of future cash flows, discount rates and volatility.

The following methods and significant assumptions have been applied in determining the fair value of financial instruments presented in the previous table, both for financial instruments carried at fair value, and those carried at cost (for which fair values are provided as a comparison):

i. The carrying value of liquid assets and other assets maturing within 12 months is assumed to be their fair value.
ii. The Bank has used a discounted cashflow methodology to arrive at the fair value for loans and advances to customers. The model used at 31 December 2012 has discounted the expected cashflows on the mortgage book based on the current market rate adjusted for various loan to value bands. An additional credit spread was included for the portion of the loans that are greater than 90% loan to value and an additional credit spread was included for buy to let and commercial loans.
iii. Derivative financial instruments used for hedging are carried on the statement of financial position at fair values, those with a positive replacement value are classified as assets and those with a negative value are classified as liabilities.
iv. Debt securities in issue are fair valued using a quoted market valuation.

While the Bank believes that its estimate of fair value is appropriate, the use of different measurements or assumptions could lead to different fair values.

Fair value measurements *

Derivative financial instruments	**2012**	**2011**
Level 1	-	-
Level 2	100%	100%
Level 3	-	-

The fair value hierarchy set out above reflects the significance of the inputs used in making the fair value measurements. Level 1 relates to quoted prices in active markets. Level 2 relates to inputs other than quoted prices that are observable either directly or indirectly. Level 3 relates to inputs which use unobservable market data. As required, the level in the fair value hierarchy within which the fair value measurement is categorised in its entirety is determined based on the lowest level of input. There are no transfers between levels 1, 2 or 3 in the Bank in respect to assets held at 31 December 2012.

Forms integral part of the audited financial statements

KPMG
Chartered Accountants
1 Harbourmaster Place
IFSC
Dublin 1
Ireland

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF EBS MORTGAGE FINANCE UNLIMITED

We have audited the financial statements of EBS Mortgage Finance Unlimited ('the Bank') for the year ended 31 December 2012 which comprise the Income Statement, the Statement of Comprehensive Income, the Statement of Financial Position, the Statement of Cash Flows, the Statement of Changes in Shareholder's Equity and the related notes. The financial reporting framework that has been applied in their preparation is Irish law and International Financial Reporting Standards (IFRSs) as adopted by the European Union as applied in accordance with the provisions of the Companies Acts 1963 to 2012.

This report is made solely to the Bank's members, as a body, in accordance with section 193 of the Companies Act 1990. Our audit work has been undertaken so that we might state to the Bank's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Bank and the Bank's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement set out on page 13 the directors are responsible for the preparation of the financial statements giving a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with Irish law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Ethical Standards for Auditors issued by the Auditing Practices Board.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Bank's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion:

- the financial statements give a true and fair view, in accordance with IFRSs as adopted by the EU, of the state of the Bank's affairs as at 31 December 2012 and of its loss for the year then ended; and
- the financial statements have been properly prepared in accordance with the Companies Acts 1963 to 2012.

KPMG, an Irish partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity

KPMG

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF EBS MORTGAGE FINANCE UNLIMITED (continued)

Matters on which we are required to report by the Companies Acts 1963 to 2012

We have obtained all the information and explanations which we consider necessary for the purposes of our audit.

The financial statements are in agreement with the books of account and, in our opinion, proper books of account have been kept by the Bank.

In our opinion the information given in the directors' report is consistent with the financial statements.

The net assets of the Bank, as stated in the statement of financial position are more than half of the amount of its called-up share capital and, in our opinion, on that basis there did not exist at 31 December 2012 a financial situation which under Section 40(1) of the Companies (Amendment) Act, 1983 would require the convening of an extraordinary general meeting of the Bank.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the Companies Acts 1963 to 2012 we are required to report to you if, in our opinion the disclosures of directors' remuneration and transactions specified by law are not made.

Killian J Croke

Killian Croke
for and on behalf of
KPMG
Chartered Accountants, Statutory Audit Firm
1 Harbourmaster Place
IFSC
Dublin 1

26 March 2013

Accounting policies

1.1 Reporting Entity

EBS Mortgage Finance (the 'Bank') was incorporated in the Republic of Ireland on 30 October 2008 as an unlimited company and commenced trading on 1 December 2008 operating under the Irish Central Bank Act, 1971 (as amended) and as a designated mortgage credit institution under the Asset Covered Securities Acts. The Bank is a wholly owned subsidiary of EBS Limited (formally EBS Building Society), is part of the EBS and AIB Group (the 'Group') and is regulated by the Central Bank of Ireland. The principal activities of the Bank are described in note 1.

On 1 July 2011 EBS Building Society was demutualised pursuant to the Building Societies Act 1989 (amended) and converted to EBS Limited, a private limited company pursuant to the Companies Act 1963 (as amended) under the terms of an Acquisition Conversion Scheme (the 'Scheme) completed on 1 July 2011. Under the terms of the Scheme the special investment shares issued by the Society were converted to ordinary shares in EBS Limited. 100% of the issued ordinary shares in EBS Limited held by the Minister for Finance were acquired by Allied Irish Banks, p.l.c. ('AIB') on 1 July 2011.

The Bank is a covered institution within the meaning of the Government Guarantee Scheme ('the Scheme') and stood specified under the Credit Institutions (Financial Support) (Specification of Institutions) Order 2008 (Statutory Instrument No. 416 of 2008) ('CIFS') for the period 30 September 2008 to 29 September 2010. The Bank is not a participating institution under the new Credit Institutions (Eligible Liabilities Guarantee) Scheme 2009 which came into effect on 9 December 2009.

The Bank is currently a participating institution under the National Asset Management Agency Act 2009. However, there were no mortgage loans transferred under the Act.

1.2 Statement of compliance

The financial statements have been prepared in accordance with International Accounting Standards and International Financial Reporting Standards (collectively 'IFRS') both as issued by the International Accounting Standards Board ('IASB') and subsequently adopted by the European Union ('EU') and applicable for the year ended 31 December 2012. The accounting policies have been consistently applied by Group entities and are consistent with the previous year, unless otherwise described. The financial statements also comply with the requirements of Irish Statute comprising the Companies Acts 1963 to 2012 and the European Communities (Credit Institutions: Accounts) Regulations, 1992 (as amended) and the Asset Covered Securities Acts 2001 and 2007.

1.3 Basis of preparation

The financial statements are presented in euro (€), which is the functional currency of the Bank, rounded to the nearest one million.

The financial statements have been prepared on an historical cost basis, except for derivative contracts all of which are measured at fair value. The carrying value of recognised assets and liabilities that are hedged are adjusted to record changes in the fair value attributable to the risks that are being hedged.

The financial statements comprise the income statement, the statement of comprehensive income, the statement of financial position, the statement of cash flows and the statement of changes in shareholders' equity together with the related notes. These notes also include financial instrument related disclosures which are required by IFRS 7 and revised IAS 1.

Comparative figures have been adjusted where necessary to conform with changes in presentation where additional analysis has been provided in the current year. This has resulted in the reclassification of €6m interest expense from Interest and similar income to the Net trading expense line in the Income Statement for 2011.

Accounting policies *(continued)*

GOING CONCERN

The Bank's activities are subject to risk factors as set out in the Risk Management Report. The continued financial crisis has increased these risk factors.

The financial statements have been prepared on a going concern basis.

In making its going concern assessment, the Bank's Directors have considered the economic, political and market risks and uncertainties currently impacting Irish financial institutions, including EBS Group (the 'Group'). In particular these relate to challenges in terms of liquidity, funding and capital. The Bank is dependent on the financial support from its parent, EBS Limited, who in turn is dependent on the ultimate parent, Allied Irish Banks p.l.c, to meet its capital requirements and ultimately its funding requirements. Since 1 July 2011 EBS Group has received the full support of AIB p.l.c. in meeting the necessary capital and funding requirements and for the full year 2012 the Bank has received the full support of EBS in meeting its necessary capital and funding requirements.

The financial statements have been prepared on a going concern basis on the basis of the assessment of the above mentioned risks and the commitment from Allied Irish Banks p.l.c. to support the funding and capital needs of the EBS Group and similarly the commitment from EBS to support the funding and capital needs of the Bank. In making this assessment the Directors have considered the basis on which AIB Group concluded that it is appropriate to prepare its own financial statements for the year ended 31 December 2012 on a going concern basis.

Extract from the AIB p.l.c. Annual report and financial statements for the year ended 31 December 2012 (on this extract the Group refers to AIB Group)

Going concern

The financial statements have been prepared on a going concern basis as the Directors are satisfied, having considered the risks anduncertainties impacting the Group, that it has the ability to continue in business for the foreseeable future.

In making its assessment, the Directors have considered a wide range of information relating to present and future conditions. These have included financial plans, cash flow and funding forecasts, capital resources projections, all of which have been prepared under base and stress scenarios. In addition, the Directors have considered the commitment of support provided to AIB by the Irish Government through the programme for restructuring the Irish banking system with AIB designated as one of the two 'Pillar Banks'. Furthermore, the Directors have considered the outlook for the Irish economy, taking into account such factors as progress on improving the fiscal situation and the support provided by the EU/IMF to Ireland. The Directors also considered the Eurozonesovereign debt crisis in its assessment of the going concern basis.

Background

The deterioration in the Irish economy culminated in the EU/IMF Programme of Financial Support for Ireland. This deterioration, which persisted throughout 2010 and 2011 presents significant risks and challenges for the Group in the years ahead:

The funding position of the Group has been impacted by:

- *The downgrading of the Group and sovereign credit ratings;*
- *The withdrawal of the Irish Government from the funding markets; and*
- *The EU/IMF Programme of Financial Support and the consequent withdrawal of funds from Irish banks.*

Accounting policies ***(continued)***

The EU/IMF Programme provided for the restructuring and reorganisation of the Irish banks. The subsequent Financial Measures Programme published by the Central Bank in March 2011 set a PCAR requirement for AIB (including EBS) to raise capital amounting to € 14.8 billion. This requirement was met by the end July 2011 through liability management exercises and Government capital injections (€ 5 billion by way of an equity placing; a capital contribution of € 6.1 billion; and € 1.6 billion by way of a Contingent Capital Notes issuance).

Since 2010 and through 2011, AIB has had limited access to wholesale funding and has been dependant on secured funding from the European Central Bank ("ECB") and has utilised non standard facilities from the Central Bank for a limited period. The Bank ceased using non-standard facilities in April 2011. Breaches of liquidity ratios up to July 2011 were remedied as new capital was injected by the Government. However, AIB's ECB repo funding has continued, since October 2010, to exceed a regulatory limit of 25%.

Market volatility remained elevated and liquidity depressed during 2011 driven by the deterioration in global credit markets as sovereign difficulties in the eurozone grew and the overall global macroeconomic environment remained uncertain. Credit spreads widened sharply, especially in the second half of the year, for certain countries within the Eurozone. This negative sentiment impacted on access to wholesale funding for certain sovereigns and credit institutions across Europe.
At different stages since the beginning of 2011, European leaders reaffirmed their commitment to the euro:
- On 21 July 2011, a statement by the Heads of State or Government of the euro area and EU institutions reaffirmed their commitment to the euro and to do whatever was needed to ensure the financial stability of the euro area as a whole and its
Member States;
- ECB decided to actively implement its Securities Markets Programme i.e. to intervene in the euro area public and private debt securities markets (to ensure depth and liquidity in those market segments which are dysfunctional);
- On 9 December 2011, the Heads of State or Government of the euro area and European Council agreed a package of measures to restore confidence in the financial markets which included:
- a new fiscal compact and the strengthening of stabilisation tools for the euro area including a more effective European Financial Stability Facility ("EFSF");
- the bringing forward of the implementation of the European Stability Mechanism ("ESM"); and
- a solution for the unique challenges faced by Greece.
- On 21 February 2012, European leaders agreed a second bail-out package for Greece in order to secure Greece's future in theeuro area.
These various measures, adopted since the beginning of 2011, are indicative of the commitment of all euro area Member States to save the euro and to support euro area members.

Capital
Under the EU/IMF Programme and the subsequent Financial Measures Programme published by the Central Bank in March 2011, which detailed the outcome of its review of capital (PCAR) and funding (PLAR), AIB was set a minimum capital target of 10.5% core
tier 1 in the base scenario, and a 6% core tier 1 in the stress scenario, plus an additional protective buffer which could be in the form of contingent capital. The total PCAR requirement for AIB (including EBS) was € 14.8 billion. This requirement was met by the end July 2011 as outlined above. The Group's core tier 1 ratio at 31 December 2011 is 17.9% (2010: 4%). The Group's total capital ratio at 31 December 2011 is 20.5% (2010: 9.2%).

Accounting policies *(continued)*

AIB has passed the European Banking Authority ("EBA") stress test in July 2011 and the EBA capital exercise in December 2011 (which incorporated a capital buffer for sovereign exposures) without any further capital being required.

The Directors have reviewed the capital and financial plans for the period of assessment and believe that the capital resources are sufficient to ensure that the Group is adequately capitalised both in a base and stress scenario.The Irish Government, as AIB's primary shareholder, has confirmed its recognition of AIB as a pillar bank, given its key role in supporting the Irish economy. In support of this role it has ensured that AIB has been sufficiently capitalised to meet the capital targets set by the Central Bank of Ireland through its 2011 PCAR and PLAR assessment.

Liquidity and funding

The Group's balance sheet saw significant change in 2011 arising from: the disposal of BZWBK; the acquisition of NAMA senior bonds and the deposit business from Anglo Irish Bankcorp ('Anglo'); the acquisition of EBS; the recapitalisation in July and asset deleveraging in the Non-Core segment. These changes reduced the funding requirement of AIB by € 10 billion in 2011. The cash proceeds from the sale of BZWBK, the State deposit in advance of the Government capital injection and the issuance of Own Use Bank Bonds (i.e. self issued MTN under the Government guarantee) enabled AIB exit non standard facilities in April 2011.

Nonetheless, the Group remains heavily dependent on Central Bank/ECB support, which amounted to € 31 billion (including EBS) at 31 December 2011 down from € 37 billion (AIB only) at 31 December 2010. AIB's access to wholesale funding markets continued to be restricted in 2011. This is a result of the continued negative sentiment towards the IMF/ECB bail out in the first half of 2011, the Europe-wide uncertainty in the second half of 2011 and the Group's credit rating. This increases the requirement for AIB to maintain/increase its deposit franchise, deleverage its balance sheet enabling reduction in wholesale funding dependency.

Customer deposits remain the largest source of funding for the Group. Excluding the Anglo and EBS deposits, plus the impact of the NTMA deposits at June 2011, the Group's deposits were broadly stable in the second half of 2011, notwithstanding the uncertainty Europe-wide in the latter months of the year. While the Irish Sovereign's credit rating was downgraded in 2011 and contagion has spread to the broader euro area, the Irish Sovereign has been able to distinguish itself from the other peripheral countries. In particular, the Irish Government has met the fiscal requirements and the recapitalisation of its banks as part of its EU/IMF Programme which has resulted in bond yields significantly tightening since July 2011.

Notwithstanding the 2011 improvements, it is expected that the Group will continue to be reliant on the monetary authorities for funding during the assessment period. However, AIB's access to Central Bank funding support as required is considered to be assured due to its position as one of the two 'Pillar Banks' and in particular by the announcements by the ECB and the Minister for Financeon 31 March 2011 to the effect that the required Central Bank funding would be made available. Furthermore, the ECB confirmed that the Eurosystem would continue to provide liquidity to banks in Ireland, including AIB.

Furthermore, the Group have had discussions with the Central Bank and it sought assurance of the continued availability of therequired liquidity from the Eurosystem during the period of assessment for the going concern statement. The Directors are satisfied based on the clarity of confirmations received from the Central Bank and public announcements by ECB, EU and IMF, that in all reasonable circumstances, the required liquidity and funding from the Central Bank/ECB will be available to the Group during the period of assessment.

Accounting policies *(continued)*
The Directors, therefore consider that the funding and liquidity position of AIB is assured during the assessment period.

Conclusion
On the basis of the above, the Directors believe that it is appropriate to prepare the financial statements on a going concern basis having concluded that there are no material uncertainties related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern over the period of assessment.

On the basis of the continued availability of funding from A.I.B. p.l.c. to EBS Mortgage Finance the Directors of the Bank consider that it is appropiate to prepare the financial statements on a going concern basis at this time.

1.4 Critical Accounting Judgements and Estimates
The preparation of financial statements requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of certain assets, liabilities, revenues and expenses, and disclosures of contingent assets and liabilities. The estimates and assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Since management's judgement involves making estimates concerning the likelihood of future events, the actual results could differ from those estimates.

Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future period affected.

Full details of the significant accounting policies are set out below.

The bank believes that of its significant accounting policies and estimation techniques, the following may involve a higher degree of judgement and complexity.

(i) Impairment losses on loans and advances
The Bank has purchased mortgage loans from EBS, which are secured on residential property. Where there is a risk that the Bank will not receive full repayment of the amount advanced, provisions are made in the financial statements to reduce the carrying value of loans and advances to the amount expected to be recovered.

The Bank considers that the provisions for loan impairments at 31 December 2012 were adequate based on information available at that time. However, actual losses may differ as a result of changes in collateral values, the timing and amounts of cash flows or other economic events.

The estimation of loan losses is inherently uncertain and depends upon many factors, including loan loss trends, portfolio grade profiles, local and international economic climates, conditions in various industries to which the Bank is exposed and other external factors such as legal and regulatory requirements.

Credit risk is identified, assessed and measured through the use of credit rating and scoring tools. Special attention is paid to lower quality rated loans and when appropriate, loans are transferred to specialist units to help avoid default, or where in default, to help minimise loss.

Accounting policies ***(continued)***

The management process for the identification of loans requiring provision is underpinned by independent tiers of review. Credit quality and loan loss provisioning are independently monitored by credit and risk management on a regular basis. The Bank assess and approves its provisions and provision adequacy on a quarterly basis. These provisions are in turn reviewed and approved by the AIB Group Credit Committee on a quarterly basis with ultimate Group levels being approved by the Audit Committee and the Board.

Key assumptions underpinning the estimates as if colletive and INBR provisioning are assessed annually with the benefit of experience.

Specific provisions
A specific provision is made against problem loans when, in the judgement of management, the estimated repayment realisable from the obligor, including the value of any security available, is likely to fall short of the amount of principal and interest outstanding on the obligor's loan account. The amount of the specific provision made in the Bank's financial statements is intended to cover the difference between the assets' carrying value and the present value of estimated future cash flows discounted at the assets' original effective interest rates. Specific provisions are created for cases that are individually significant, and also collectively for assets that are impaired but not individually significant.

The amount of an individually assessed specific provision required is highly dependent on estimates of the amount of future cash flows and their timing. Individually insignificant loans are collectively evaluated for impairment. As this process is model driven, based on historic loan recovery rates, the total amount of the Bank's impairment provisions on these loans is somewhat uncertain as it may not totally reflect the impact of the prevailing market conditions. However, the recovery rates are updated at a minimum on a yearly basis.

Changes in the estimate of the value of security and the time it takes to receive those cash flows could have a significant effect on the amount of impairment provisions required and on the income statement expense and balance sheet position, for example, in assessing the value of residential property held as collateral for impaired mortgage loans in Ireland, EBS Mortgage Finance uses a 'peak to trough' house price decline of 55% as a base. In certain circumstances, realisation costs of 10% to 20% are also deducted. For larger impaired loans (individually significant) other factors such as recent transactional evidence and/or local knowledge are considered, which can result in higher discounts to collateral values. CSO statistics for December 2012 outline a 'peak to trough' decline of 49.6% for residential property, nationally. If prices were to decline by a further 5% from EBS Mortgage Finance 's assumed values (resulting in a cumulative peak to trough fall of 58%) and this decline fell directly through to the collateral values of its impaired mortgage loans in Ireland, the additional impairment provision impact would be in the range of approximately €16 million to €18 million.

Incurred but not reported provisions
Incurred but not reported ("IBNR") provisions are also maintained to cover loans which are impaired at the reporting date and, while not specifically identified, are known from experience to be present in any portfolio of loans. IBNR provisions are maintained at levels that are deemed appropriate by management having considered: credit grading profiles and grading movements; historic loan loss rates; changes in credit management; procedures, processes and policies; levels of credit management skills; local and international economic climates; portfolio sector profiles/industry conditions; and current estimates of loss in the portfolio.

Accounting policies ***(continued)***

The total amount of impairment loss in the Bank's non-impaired portfolio and therefore the adequacy of the IBNR allowance is inherently uncertain. There may be factors in the portfolio that have not been a feature of the past and changes in credit grading profiles and grading movements may lag the change in the credit profile of the customer. In addition, current estimates of loss within the earning portfolio and the period of time it takes following a loss event for an individual loan to be recognised as impaired ('emergence period') are subject to a greater element of estimation due to the speed of change in the economies in which the Group operates and the unprecedented market conditions.

Forbearance
The Bank has developed a number of forbearance strategies for both short-term and longer-term solutions to assist customers experiencing financial difficulties. The forbearance strategies involve modifications to contractual repayment terms in order to improve the collectability of outstanding debt, to avoid default, and where relevant, to avoid repossessions. The longer-term advanced forbearance strategies are currently in the process of being rolled to relevant residential mortgage customers in Ireland, accordingly, a higher level of judgement and estimation is involved in determining their effects on impairment provisions.

(ii) Effective interest rate
Interest income and expense is recognised in the Income Statement for all interest-bearing financial instruments using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset or liability (or group of assets and liabilities) and of allocating the interest income or interest expense over the relevant period. The effective interest rate at origination is the rate that exactly discounts the expected future cash payments or receipts through the expected life of the financial instrument, or when appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. The application of the method has the effect of recognising income (and expense) receivable (or payable) on the instrument evenly in proportion to the amount outstanding over the period to maturity or repayment.

In calculating the effective interest rate, the Bank estimates cash flows (using projections based on its experience of customers' behaviour) considering all contractual terms of the financial instrument but excluding future credit losses. This critical accounting policy is assessed on an annual basis and any changes are charged/ credited to the income statement.

(iii) Derivatives financial instruments
The Bank uses derivative financial instruments to hedge its exposure to interest rate risks. In accordance with treasury policy, the Bank does not hold or issue derivative financial instruments for trading purposes.

Derivative financial instruments are recognised initially at fair value. Subsequent to initial recognition, derivative financial instruments are stated at fair value. The gain or loss on re-measurement to fair value is recognised immediately in the income statement. However, where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the hedge relationship.

The fair value of derivative financial instruments is the estimated amount that the Bank would receive or pay to terminate the instrument at the reporting date. Interest rate swaps are valued by calculating the net present value of the cash flows over the life of the swap. All derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

Accounting policies *(continued)*

(iv) Deferred taxation

Deferred tax assets are recognised for unused tax losses to the extent that it is probable (defined for this purpose as more likely than not) that there will be sufficient future taxable profits against which the losses can be used. For a company with a history of recent losses, there must be convincing other evidence to underpin this assessment. The recognition of the deferred tax asset relies on the assessment of future profitability and the sufficiency of those profits to absorb losses carried forward. It requires significant judgements to be made about the projection of long-term future profitability because of the period over which recovery extends.

In assessing the future profitability of the Bank, the Board has considered a range of positive and negative evidence.

Among this evidence, the principal positive factors include the:

- absence of any expiry dates for Irish tax losses;
- non-enduring nature of the loan impairments at levels which resulted in recent years' losses;
- generation of operating profits before provisions in recent years; and
- return to profitability within the Bank's internal medium-term financial plan and the ability to grow profits thereafter.

Taking account of all relevant factors the Bank believes that it is more likely than not that it will return to profitability within the timescale of the Bank's medium-term financial plan and will achieve profits producing a sustainable market-range return on equity in the long term. In the absence of any expiry date for tax losses in Ireland, the Bank therefore believes that it is more likely than not that there will be future profits against which to use the tax losses.

IAS 12 does not permit a company to apply present value discounting to its deferred tax assets or liabilities, regardless of the estimated timescales over which those assets or liabilities are projected to be realised. The Bank's deferred tax assets are projected to be realised over a long timescale, benefiting from the absence of any expiry date for Irish tax losses. As a result, the carrying value of the deferred tax assets on the statement of financial position does not reflect the economic value of those assets.

Adoption of new accounting standards

The following amendments to standards have been adopted by the Bank during the year ended 31 December 2012.

<u>Disclosures – Transfers of Financial Assets (Amendments to IFRS 7)</u>

This amendment to IFRS 7 requires certain disclosures in respect of all transferred financial assets that are not derecognised in their entirety and transferred assets that are derecognised in their entirety but with which there is continuing involvement including the possible effects of any risks that may remain with the transferor of the assets. This requirement has not has an impact on the Bank's financial statements for the year ended 31 December 2012.

1.5 Interest Income and Expense Recognition

Interest income and expense is recognised in the income statement for all interest-bearing financial instruments using the effective interest method.

Accounting policies *(continued)*

The effective interest method is a method of calculating the amortised cost of a financial asset or financial liability (or group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts the estimated future cash payments or receipts through the expected life of the financial instrument to the net carrying amount of the financial asset or financial liability. The application of the method has the effect of recognising income or expense on the instrument evenly in proportion to the amount outstanding over the period to maturity or repayment.

In calculating the effective interest rate, the Bank estimates cash flows (using projections based on its experience of customers' behaviour) considering all contractual terms of the financial instrument but excluding future credit losses. The calculation takes into account all fees, including those for early redemption, and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums and discounts.

All costs associated with mortgage incentive schemes are included in the effective interest rate calculation. Fees and commissions payable to third parties in connection with lending arrangements, where these are direct and incremental costs related to the issue of a financial instrument, are included in interest income as part of the effective interest rate.

Interest income and expense presented in the income statement includes:-

- Interest on financial assets and financial liabilities at amortised cost on an effective interest method; and
- Net interest income and expense on qualifying hedge derivatives designated as cash flow hedges or fair value hedges which are recognised in interest income or interest expense.

1.6 Net Trading Income

Net trading income comprises gains less losses relating to trading assets and trading liabilities and includes all realised and unrealised fair value changes.

1.7 Non-credit Risk Provisions

Provisions are recognised for present legal or constructive obligations arising as consequences of past events where it is probable that a transfer of economic benefit will be necessary to settle the obligation, and it can be reliably estimated.

When the effect is material, provisions are determined by discounting expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Payments are deducted from the present value of the provision and interest, at the relevant discount rate, is charged annually to interest expense using the effective interest method. Changes in the present value of the liability as a result of movements in interest rates are included in other financial income. The present value of provisions is included in other liabilities.

1.8 Income Tax, including Deferred Income Tax

Income tax comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised in other comprehensive income, in which case it is recognised in other comprehensive income. Income tax relating to items in equity is recognised directly in equity.

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

Accounting policies *(continued)*

Deferred income tax is provided, using the financial statement liability method, on temporary differences between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred income tax is determined using tax rates based on legislation enacted or substantively enacted at the reporting date and expected to apply when the deferred tax asset is realised or the deferred tax liability is settled. Deferred income tax assets are recognised when it is probable that future taxable profits will be available against which the temporary differences will be utilised.

The tax effects of income tax losses available for carry forward are recognised as an asset when it is probable that future taxable profits will be available against which these losses can be utilised.

Deferred and current tax assets and liabilities are only offset when they arise in the same tax reporting group and where there is both the legal right and the intention to settle the current tax assets and liabilities on a net basis or to realise the asset and settle the liability simultaneously. The principal temporary differences arise from revaluation of certain financial assets and financial liabilities including derivative contracts.

1.9 Impairment of Financial Assets

It is Bank's policy to make provisions for impairment of financial assets to reflect the losses inherent in those assets at the reporting date.

Impairment

The Bank assesses at each reporting date whether there is objective evidence that a financial asset or a portfolio of financial assets are impaired. A financial asset or portfolio of financial assets are impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more loss events that occurred after the initial recognition of the asset and on or before the reporting date ('a loss event'), and that loss event or events has had an impact such that the estimated present value of future cash flows is less than the current carrying value of the financial asset, or portfolio of financial assets.

Objective evidence that a financial asset or a portfolio of financial assets are impaired includes observable data that comes to the attention of the Bank about the following loss events:

a) significant financial difficulty of the issuer or obligor;
b) a breach of contract, such as a default or delinquency in interest or principal payments;
c) the granting to the borrower of a concession, for economic or legal reasons relating to the borrower's financial difficulty that the Bank would not otherwise consider;
d) it becomes probable that the borrower will enter bankruptcy or other financial reorganisation;
e) the disappearance of an active market for that financial asset because of financial difficulties; or
f) observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the portfolio, including:
   i. adverse changes in the payment status of borrowers in the portfolio;
   ii. national or local economic conditions that correlate with defaults on the assets in the portfolio.

Accounting policies *(continued)*

Incurred but not reported

The Bank first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and collectively for financial assets that are not individually significant (i.e. individually insignificant). If the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset under the collective incurred but not reported ('IBNR') assessment. A collective impairment provision represents an interim step pending the identification of impairment losses on an individual asset in a group of financial assets. As soon as information is available that specifically identifies losses on individually impaired assets in a group, those assets are removed from the group. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

Collective evaluation of impairment

For the purpose of collective evaluation of impairment (individually insignificant impaired assets and collective), financial assets are grouped on the basis of similar risk characteristics. These characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the counterparty's ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Future repayment behaviour for a group of financial assets that are collectively evaluated for impairment is assessed on the basis of the historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not currently exist.

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

Impairment loss

For loans and advances and assets held to maturity, the amount of impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate. The amount of the loss is recognised using an allowance account and is included in the income statement.

Following impairment, interest income is recognised using the original effective rate of interest which was used to discount the future cash flows for the purpose of measuring the impairment loss. 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, the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement.

When a loan has been subjected to a specific provision and the prospects of recovery do not improve, a time will come when it may be concluded that there is no real prospect of recovery. When this point is reached, the amount of the loan which is considered to be beyond the prospect of recovery is written off against the related provision for loan impairment. Subsequent recoveries of amounts previously written off decrease the amount of the provision for loan impairment in the income statement.

Assets acquired in exchange for loans and advances in order to achieve an orderly realisation are accounted for as a disposal of the loan and an acquisition of an asset. Any further impairment of the assets or business acquired is treated as an impairment of the relevant asset and not as an impairment of the original instrument.

Accounting policies ***(continued)***

Loans renegotiated and forbearance
From time to time, the Bank will modify the original terms of a customer's loan either as part of the on-going relationship with the customer or arising from changes in the customer's circumstances such that he is unable to make the agreed original contractual repayments.

Forbearance
A forbearance agreement is entered into where the customer is in financial difficulty to the extent that they are unable to repay both the principal and interest on their loan in accordance with their original contract. Following an assessment of the customer's repayment capacity, a potential solution will be determined from the options available. A request for a forbearance solution acts as a trigger for an impairment test under IAS 39 as it may confirm that a loss event has occurred. There are a number of different types of forbearance options including interest and/or arrears capitalisation, interest rate adjustments, payment holidays, term extensions and split loans.

All loans that are assessed for a forbearance solution are tested for impairment under IAS 39 and where a loan is deemed impaired, an appropriate provision is raised to cover the difference between the loan's carrying value and the present value of estimated future cash flows discounted at the loan's original effective interest rate. Where, having assessed the loan for impairment and the loan is not deemed to be impaired, it is included within the collective assessment as part of the IBNR provision calculation.

Forbearance loans classified as impaired may be upgraded from impaired status to performing status where the borrower displays a satisfactory performance following the period of restructure of the loan, comprising a minimum period of 12 months consecutive payments of the new contractually agreed terms, typically being full principal and interest. Where loans are upgraded from impaired, they are included in the Bank's collective assessment for impairment provisioning (IBNR).

Where the terms on a renegotiated loan which has been subject to an impairment provision differ substantially from the original loan terms either in a quantitative or qualitative analysis, the original loan is derecognised and a new loan is recognised at fair value. Any difference between the carrying amount of the loan and the fair value of the new renegotiated loan terms is recognised as an additional impairment provision. Interest accrues on the new loan based on the current market rates.

Non-forbearance renegotiation
Occasionally, the Bank may temporarily amend the contractual repayments term on a loan (e.g. payment moratorium) for a short period of time due to a temporary change in the life circumstances of the borrower. Because such events are not directly linked to repayment capacity, these amendments are not considered forbearance. The changes in expected cash flows are accounted for under IAS 39.AG8 i.e. the carrying amount of the loan is adjusted to reflect the revised estimated cash flows which are discounted at the original effective interest rate. Any adjustment to the carrying amount of the loan is reflected in the income statement as interest income/expense.

Where the terms on a renegotiated loan differ substantially from the original loan terms either in a quantitative or qualitative analysis, the original loan is derecognised and a new loan is recognised at fair value. Any difference arising between the derecognised loan and the new loan is recognised in the income statement.

Where a customer's request for a modification to the original loan agreement is deemed not to be a forbearance request (i.e. the customer is not in financial difficulty to the extent that they are unable to repay both the principal and interest), these loans are not disaggregated for monitoring/reporting of IBNR assessment purposes.

Accounting policies *(continued)*

Collateralised financial assets
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, costs for obtaining and settling the collateral, and whether or not foreclosure is probable.

Past due loans
When a borrower fails to make a contractually due payment, a loan is deemed to be past due. "Past due days" is a term used to describe the equivalent cumulative numbers of days that a missed payment is overdue. For loans paying interest in advance, past due days commence from the close of business on the last day of the month in which a payment is due but not received. For loans paying interest in arrears, past due days commence from the close of business on the day on which a payment is due but not received. When a borrower is past due, the entire exposure is reported as past due, rather than the amount of any excess or arrears.

Loans and advances renegotiated
Loans and advances renegotiated are those facilities outstanding at the reporting date that, during the financial year have had their terms renegotiated, resulting in an upgrade from 90+ days past due or impaired status to performing status.

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

1.10 Determination of Fair Value of Financial Instruments
The fair value of a financial instrument is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Financial assets are initially recognised at fair value and, with the exception of financial assets at fair value through profit or loss, the initial fair value includes direct and incremental transaction costs. Financial liabilities are initially recognised at fair value, being their issue proceeds (fair value of consideration received) net of transaction costs incurred. Subsequent to initial recognition, the methods used to determine the fair value of financial instruments include quoted prices in active markets where those prices are considered to represent actual and regularly occurring market transactions on an arm's length basis. Where quoted prices are not available or are unreliable because of market inactivity, fair values are determined using valuation techniques. These valuation techniques which use, to the extent possible, observable market data, include the use of recent arm's length transactions, reference to other similar instruments, option pricing models and discounted cash flow analysis and other valuation techniques commonly used by market participants.

Quoted prices in active markets
Quoted market prices are used where those prices are considered to represent actual and regularly occurring market transactions on an arm's length basis, in active markets.

Accounting policies ***(continued)***

Valuations for negotiable instruments, such as debt and equity securities, are determined using bid prices for asset positions and offer prices for liability positions. Where securities are traded on an exchange, the fair value is based on prices from the exchange. The market for debt securities largely operates on an "over the counter" basis which means that there is not an official clearing or exchange price for these security instruments. Therefore, market makers and/or investment banks ('contributors') publish bid and offer levels which reflect an indicative price that they are prepared to buy and sell a particular security. The Group's valuation policy requires that the prices used in determining the fair value of securities quoted in active markets must be sourced from established market makers and/or investment banks.

Valuation techniques
In the absence of quoted market prices, or in the case of over-the-counter derivatives, fair value is calculated using valuation techniques. Fair value may be estimated using quoted market prices for similar instruments, adjusted for differences between the quoted instrument and the instrument being valued. Where the fair value is calculated using discounted cash flow analysis, the methodology is to use, to the extent possible, market data that is either directly observable or is implied from instrument prices, such as interest rate yield curves, equities and commodities prices, credit spreads, option volatilities and currency rates. In addition, the Bank considers the impact of own credit risk when valuing its derivative liabilities.

The methodology is to calculate the expected cash flows under the terms of each specific contract and then discount these values back to a present value. The assumptions involved in these valuation techniques include:-

- The likelihood and expected timing of future cash flows of the instrument. These cash flows are generally governed by the terms of the instrument, although management judgement may be required when the ability of the counterparty to service the instrument in accordance with the contractual terms is in doubt. In addition, future cash flows may also be sensitive to the occurrence of future events, including changes in market rates; and
- Selecting an appropriate discount rate for the instrument, based on the interest rate yield curves including the determination of an appropriate spread for the instrument over the risk-free rate. The spread is adjusted to take into account the specific credit risk profile of the exposure.

Certain financial instruments may be valued on the basis of valuation techniques that feature one or more significant market inputs that are not observable. When applying a valuation technique with unobservable data, estimates are made to reflect uncertainties in fair values resulting from a lack of market data, for example, as a result of illiquidity in the market. For these instruments, the fair value measurement is less reliable. Inputs into valuations based on non-observable data are inherently uncertain because there is little or no current market data available from which to determine the level at which an arm's length transaction would occur under normal business conditions. However, in most cases there is some market data available on which to base a determination of fair value, for example historical data, and the fair values of most financial instruments will be based on some market observable inputs even where the non-observable inputs are significant.
The Bank tests the outputs of the model to ensure that it reflects current market conditions. The calculation of fair value for any financial instrument may require adjustment of the quoted price or the valuation technique output to reflect the cost of credit risk, the liquidity of the market, and hedging costs where these are not embedded in underlying valuation techniques or prices used.

The choice of contributors, the quality of market data used for pricing, and the valuation techniques used are all subject to internal review and approval procedures.

Accounting policies *(continued)*

1.11 Financial Assets

The Bank classifies its financial assets into the following categories: - financial assets at fair value through profit or loss and loans and advances.

Purchases and sales of financial assets are recognised on trade date, being the date on which the Bank commits to purchase or sell the assets. Loans are recognised when cash is advanced to the borrowers.

Interest is calculated using the effective interest method and credited to the income statement. Dividends on available-for-sale equity securities are recognised in the income statement when the entity's right to receive payment is established. Impairment losses and translation differences on monetary items are recognised in the income statement.

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or when the Group has transferred substantially all the risks and rewards of ownership.

Financial assets at fair value through profit or loss

This category can have two sub categories: - Financial assets held for trading; and those designated at fair value through profit or loss at inception. A financial asset is classified in this category if it is acquired principally for the purpose of selling in the near term; part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit taking; or if it is so designated at initial recognition by management, subject to certain criteria.

The assets are recognised initially at fair value and transaction costs are taken directly to the income statement. Interest and dividends on assets within this category are reported in interest income, and dividend income, respectively. Gains and losses arising from changes in fair value are included directly in the income statement within net trading income. Derivatives are also classified in this category unless they have been designated as hedges or are financial guarantee contracts.

Loans and advances

Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and which are not classified as available-for-sale. They arise when the Bank provides money or services directly to a customer with no intention of trading the loan. Loans and advances are initially recognised at fair value including direct and incremental transaction costs and are subsequently carried on an amortised cost basis.

1.12 Financial Liabilities

Issued financial instruments or their components are classified as liabilities where the substance of the contractual arrangement results in the Bank having a present obligation to either deliver cash or another financial asset to the holder, to exchange financial instruments on terms that are potentially unfavourable or to satisfy the obligation otherwise than by the exchange of a fixed amount of cash or another financial asset for a fixed number of equity shares.

Financial liabilities are initially recognised at fair value, being their issue proceeds (fair value of consideration received) net of transaction costs incurred. Financial liabilities are subsequently measured at amortised cost, with any difference between the proceeds net of transaction costs and the redemption value recognised in the income statement using the effective interest method.

Accounting policies *(continued)*

Where financial liabilities are classified as trading they are also initially recognised at fair value and the related transaction costs are taken directly to the income statement. Gains and losses arising from changes in fair value are recognised directly in the income statement within net trading income.

The Bank derecognises a financial liability when its contractual obligations are discharged, cancelled or expired. Any gain or loss on the extinguishment or re-measurement of a financial liability is recognised in profit or loss.

1.13 Intangible Assets

Intangible assets are costs associated with the set up of the Bank. They are amortised using the straight-line method over their useful life not exceeding 10 years. The amortisation expense is recognised in the Income Statement in operating expenses.

1.14 Derivatives and Hedge Accounting

Derivatives, such as interest rate swaps, are used for hedging purposes as part of the Bank's risk management strategy against assets, liabilities, positions and cash flows.

Derivatives

Derivatives are measured initially at fair value on the date on which the derivative contract is entered into and subsequently re-measured at fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and from valuation techniques using discounted cash flow models and option pricing models as appropriate. Derivatives are included in assets when their fair value is positive and in liabilities when their fair value is negative, unless there is the legal ability and intention to settle an asset and liability on a net basis.

The best evidence of the fair value of a derivative at initial recognition is the transaction price (i.e. the fair value of the consideration given or received) unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets.

Profits or losses are only recognised on initial recognition of derivatives when there are observable current market transactions or valuation techniques that are based on observable market inputs.

Hedging

All derivatives are carried at fair value and the accounting treatment of the resulting fair value gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. Where derivatives are held for risk management purposes, and where transactions meet the criteria specified in IAS 39 "Financial Instruments: Recognition and Measurement", the Bank designates certain derivatives as either:

i. hedges of the fair value of recognised assets or liabilities or firm commitments ('fair value hedge'); or
ii. hedges of the exposure to variability of cash flows attributable to a recognised asset or liability, or a highly probable forecasted transaction ('cash flow hedge').

When a financial instrument is designated as a hedge, the Bank formally documents the relationship between the hedging instrument and hedged item as well as its risk management objectives and its strategy for undertaking the various hedging transactions. The Bank also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of the hedged items.

Accounting policies ***(continued)***

The Bank discontinues hedge accounting when:
a) it is determined that a derivative is not, or has ceased to be, highly effective as a hedge;
b) the derivative expires, or is sold, terminated, or exercised;
c) the hedged item matures or is sold or repaid; or
d) a forecast transaction is no longer deemed highly probable.

To the extent that the changes in the fair value of the hedging derivative differ from changes in the fair value of the hedged risk in the hedged item; or the cumulative change in the fair value of the hedging derivative differs from the cumulative change in the fair value of expected future cash flows of the hedged item, ineffectiveness arises. The amount of ineffectiveness, (taking into account the timing of the expected cash flows, where relevant) provided it is not so great as to disqualify the entire hedge for hedge accounting, is recorded in the income statement.

In certain circumstances, the Bank may decide to cease hedge accounting even though the hedge relationship continues to be highly effective by no longer designating the financial instrument as a hedge.

Fair value hedge accounting
Changes in fair value of derivatives that qualify and are designated as fair value hedges are recorded in the income statement, together with changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. If the hedge no longer meets the criteria for hedge accounting, the fair value hedging adjustment cumulatively made to the carrying value of the hedged item is, for items carried at amortised cost, amortised over the period to maturity of the previously designated hedge relationship using the effective interest method. For available-for-sale items the fair value hedging adjustment remains in equity, until the hedged item affects the income statement and is recognised in the income statement using the effective interest method. If the hedged item is sold or repaid, the unamortised fair value adjustment is recognised immediately in the income statement.

Cash flow hedge accounting
The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is initially recognised directly in other comprehensive income and included in the cash flow hedging reserve in the statement of changes in equity. The amount recognised in other comprehensive income is re-classed to profit or loss as a reclassification adjustment in the same period as the hedged cash flows affect profit or loss, and in the same line item in the statement of comprehensive income. Any ineffective portion of the gain or loss on the hedging instrument is recognised in the income statement immediately.
When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss recognised in other comprehensive income from the time when the hedge was effective remains in equity and is reclassified to the income statement as a reclassification adjustment as the forecast transaction affects profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was recognised in other comprehensive income from the period when the hedge was effective is reclassified from equity to the income statement.

Derivatives that do not qualify for hedge accounting
Certain derivative contracts entered into as economic hedges do not qualify for hedge accounting. Changes in the fair value of derivative instruments that do not qualify for hedge accounting are recognised immediately in the income statement.

1.15 Collateral and Netting
The Bank enters into master netting agreements with counterparties, to ensure that if an event of default occurs, all amounts outstanding with those counterparties will be settled on a net basis.

Accounting policies ***(continued)***

Collateral
The Bank obtains collateral in respect of customer liabilities where this is considered appropriate. The collateral normally takes the form of a lien over the customer's assets and gives the Bank a claim on these assets for both existing and future liabilities. The collateral is, in general, not recorded on the statement of financial position.

The Bank also receives collateral in the form of cash or securities in respect of other credit instruments, such as stock borrowing contracts and derivative contracts in order to reduce credit risk. Collateral received in the form of securities is not recorded on the statement of financial position. Collateral received in the form of cash is recorded on the statement of financial position with a corresponding liability. These items are assigned to deposits received from banks or other counterparties in the case of cash collateral received. Any interest payable or receivable arising is recorded as interest expense or interest income respectively.

In certain circumstances, the Bank will pledge collateral in respect of liabilities or borrowings. Collateral pledged in the form of securities or loans and advances continues to be recorded on the statement of financial position. Collateral paid away in the form of cash is recorded in loans and advances to banks or customers. Any interest payable or receivable arising is recorded as interest expense or interest income respectively.

Netting
Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position if, and only if, there is a currently enforceable legal right to set off the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously. This is not generally the case with master netting agreements where the related assets and liabilities are presented gross on the statement of financial position.

1.16 Share Capital
Issued financial instruments, or their components, are classified as equity where they meet the definition of equity and confer on the holder a residual interest in the assets of the Bank. Incremental costs directly attributable to the issue, if any, of an equity instrument are deducted from the initial measurement of the equity instrument.

1.17 Cash and cash equivalents
For the purposes of the cash flow statement, cash comprises cash on hand and demand deposits, and cash equivalents comprise highly liquid investments that are convertible into cash with an insignificant risk of changes in value and with original maturities of less than three months.

1.18 Prospective Accounting Changes
The following new accounting standards and amendments to existing standards approved by the IASB in 2010 and 2011, but not early adopted by the Bank, will impact the Bank's financial reporting in future periods.

The following will be applied in 2013 unless otherwise noted:
Amendments to IAS 1 - Presentation of Items in Other Comprehensive Income
The amendments to IAS 1 were issued in June 2011 and are applicable to annual periods beginning on or after 1 July 2012. These amendments require companies preparing financial statements in accordance with IFRSs to group together items within other comprehensive income that may be reclassified to the profit or loss section of the income statement. The amendments also reaffirm existing requirements that items in other comprehensive income and profit or loss should be presented as either a single statement or two consecutive statements.

Accounting policies *(continued)*

IFRS 13 Fair Value Measurement

This standard, which applies prospectively for annual periods beginning on or after 1 January 2013, establishes a single source of guidance for fair value measurements under IFRSs. IFRS 13 defines fair value, provides guidance on its determination and introduces consistent requirements for disclosures on fair value measurements. IFRS 13 requires entities to disclose information about the valuation techniques and inputs used to measure fair value, as well as information about the uncertainty inherent in fair value measurements. This information will be required for both financial and non-financial assets and liabilities.

Offsetting Financial Assets and Financial Liabilities – Amendments to IAS 32, and Disclosures – Offsetting Financial Assets and Financial Liabilities – Amendments to IFRS 7

In December 2011, the IASB issued amendments to IAS 32 and IFRS 7 which clarify the accounting requirements for offsetting financial instruments and introduce new disclosure requirements that aim to improve the comparability of financial statements prepared in accordance with IFRS and US GAAP.The amendments to IFRS 7 will require more extensive disclosures than are currently required. The disclosures focus on quantitative information about recognised financial instruments that are offset in the statement of financial position, as well as those recognised financial instruments that are subject to master netting or similar arrangements, irrespective of whether they are offset. The amended offsetting disclosures are to be retrospectively applied, with an effective date of annual periods beginning on or after 1 January 2013.

The amendments to IAS 32 clarify that the right of set-off must be currently available and legally enforceable for all counterparties in the normal course of business, as well as in the event of default, insolvency or bankruptcy. The IAS 32 changes are effective for annual periods beginning on or after 1 January 2014 and apply retrospectively.

The following will be applied in 2015:

IFRS 9 Financial instruments

In 2009, the IASB commenced the implementation of its project plan for the replacement of IAS 39. This consists of three main phases:

Phase 1: Classification and measurement

In November 2009, the IASB issued IFRS 9 Financial Instruments, covering classification and measurement of financial assets, as the first part of its project to replace IAS 39 and simplify the accounting for financial instruments. The new standard endeavours to enhance the ability of investors and other users of financial information to understand the accounting for financial assets and to reduce complexity. IFRS 9 uses a single approach to determine whether a financial asset is measured at amortised cost or fair value, replacing the many different rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments (its business model) and the contractual cash flow characteristics of the financial assets.

In October 2010, the IASB reissued IFRS 9 incorporating new requirements on accounting for financial liabilities, and carrying over from IAS 39 the requirements for de-recognition of financial assets and financial liabilities. IFRS 9 does not change the basic accounting model for financial liabilities under IAS 39.Two measurement categories continue to exist: fair value through profit or loss ('FVTPL') and amortised cost. Financial liabilities held for trading are measured at FVTPL, and all other financial liabilities are measured at amortised cost unless the fair value option is applied.

IFRS 9 requires gains and losses on financial liabilities designated as at fair value through profit or loss to be split into the amount of change in the fair value that is attributable to changes in the credit risk of the liability, which should be presented in other comprehensive income, and the remaining amount of change in the fair value of the liability which should be presented in profit or loss in the income statement.

The basic premise for the de-recognition model in IFRS 9 (carried over from IAS 39) is to determine whether the asset under consideration for de-recognition is:

- an asset in its entirety; or
- specifically identified cash flows from an asset (or a group of similar financial assets); or
- a fully proportionate (pro rata) share of the cash flows from an asset (or a group of similar financial assets); or
- a fully proportionate (pro rata) share of specifically identified cash flows from a financial asset (or a group of similar financial assets).
- A financial liability should be removed from the statement of financial position when, and only when, it is extinguished, that is, when the obligation specified in the contract is either discharged or cancelled or expires.
- All derivatives, including those linked to unquoted equity investments, are measured at fair value. Value changes are recognised in profit or loss unless the entity has elected to treat the derivative as a hedging instrument in accordance with IAS 39, in which case the requirements of IAS 39 apply.

Phase 2: Impairment methodology

An exposure draft issued by the IASB in November 2009 proposes an "expected loss model" for impairment. Under this model, expected losses are recognised throughout the life of a loan or other financial asset measured at amortised cost, not just after a loss event has been identified. The expected loss model avoids what many see as a mismatch under the incurred loss model – front-loading of interest revenue (which includes an amount to cover the lender's expected loan loss) while the impairment loss is recognised only after a loss event occurs. The impairment phase of IFRS 9 is subject to on-going deliberations and has not yet been finalised.

Accounting policies ***(continued)***

Phase 3: Hedge accounting
In September 2012, the IASB posted on its website a review draft of the proposed hedge accounting requirements that will be incorporated into IFRS 9. The draft proposes a model that aims to align hedge accounting with risk management activities; and addresses inconsistencies and weaknesses in the existing model in IAS 39. This phase is expected to be finalised in the first quarter of 2013.

Since significant aspects of the standard have yet to be finalised, it is impracticable for the Bank to quantify the impact of IFRS 9 at this stage.

The new standard is still subject to EU endorsement.

Income Statement

for the year ended 31 December 2012

	Notes	2012 €m	2011 €m
Interest and similar income	2	322	236
Interest expense and similar charges	2	(202)	(177)
Net interest income	2	**120**	59
Net trading expense	3	**(10)**	(4)
Other operating loss	4	**(98)**	-
Total operating income		**12**	55
Operating expenses	5	**(8)**	(6)
Operating profit before provisions		**4**	49
Provision for impairment losses of loans and advances to customers	8	**(94)**	(128)
Operating (loss) before taxation		**(90)**	(79)
Taxation on ordinary activities	6	**12**	10
(Loss) for the financial year		**(78)**	(69)

The operating loss is derived from continuing operations.

Statement of comprehensive income

for the year ended 31 December 2012

	2012 €m	2011 €m
(Loss) for the financial year	**(78)**	(69)
Other comprehensive income	-	-
Total comprehensive (loss) for the year	**(78)**	(69)

See accompanying notes forming part of the financial statements.

On behalf of the Board :

Director

Director

Director

Company Secretary

Date : 26 March 2013

Statement of financial position

As at 31 December 2012

	Notes	2012 €m	2011 €m
Assets			
Derivative financial instruments	17	**35**	56
Loans and advances to credit institutions	7	**128**	130
Loans and advances to customers	8	**6,427**	7,176
Deferred taxation	10	**22**	10
Prepayments and accrued income	11	**-**	1
Intangible assets	9	**2**	2
Total assets		**6,614**	7,375
Liabilities			
Deposits by credit institutions	12	**3,254**	3,614
Derivative financial instruments	17	**36**	54
Accruals and deferred income	14	**2**	6
Other liabilities	15	**-**	2
Debt securities in issue	13	**2,969**	3,268
Total liabilities		**6,261**	6,944
Shareholders' equity			
Ordinary share capital	20	**477**	477
General Reserves		**(124)**	(46)
Total shareholders' equity		**353**	431
Total liabilities and shareholders' equity		**6,614**	7,375

See accompanying notes forming part of the financial statements.

On behalf of the Board :

Director

Director

Director

Company Secretary

Date : 26 March 2013

Statement of changes in equity

As at 31 December 2012

	Ordinary share capital	General reserves	Total
	€m	€m	€m
2012			
At beginning of year	477	(46)	431
Total comprehensive (loss) for the year	-	(78)	(78)
At end of year	477	(124)	(353)

	Share capital	Revenue reserves	Total
	€m	€m	€m
2011			
At beginning of year	317	23	340
Ordinary share capital issued	160	-	160
Total comprehensive (loss) for the year	-	(69)	(69)
At end of year	477	(46)	431

Statement of Cashflow *for the year ended 31 December 2012*	Note	2012 €m	2011 €m
Cash flows from operating activities			
Operating (loss) before taxation		**(90)**	(79)
Adjustments for:			
Amortisation of premium/discount		**82**	39
Provision for impairment of loans and advances	8	**94**	130
Loss on disposals of loans	4	**152**	-
Gain on repurchase of debt securities in issue	4	**(54)**	-
Fair value movement on hedging derivatives		**(1)**	6
Fair value movement on hedged item		**4**	(6)
Operating income before changes in working capital and provisions		**187**	90
Net (decrease) increase in loans and advances to customers	8	**503**	(1,951)
Net increase in prepayments and accrued income	11	**1**	-
(Decrease) increase in other liabilities		**(2)**	738
(Decrease) increase in deposits by credit institutions	12	**(360)**	740
Increase/(decrease) in accrual and deferred income	14	**(4)**	-
Cash used in operations		**325**	(1,123)
Income taxes refunded		-	-
Net cash used in operating activities		**325**	(1,123)
Net cash outflow from investing activities			
Cash flows from financing activities			
Issue of debt securities	13	**985**	1,010
Redemption of debt securities	13	**(1,312)**	-
Issue of share capital	20	-	160
Net (outflow) cash inflow from financing activities		**(327)**	1,170
Net increase in cash and cash equivalents		**(2)**	47
Cash and cash equivalents at beginning of period		**130**	83
Cash and cash equivalents at 31 December	7	**128**	**130**

Notes to the accounts

1. REPORTING BY BUSINESS SEGMENTS AND GEOGRAPHICAL LOCATION

The Bank's activities are carried out exclusively in the financial services sector in the Republic of Ireland. The Bank does not sell mortgage loans directly to the public. It has an origination agreement with EBS whereby EBS continues to sell mortgage loans directly to the public and subsequently sell pools of loans to the Bank for an appropriate consideration.

For management and reporting purposes the Bank's activities are organised in one reportable segment based on the information provided internally to the chief operating decision maker. The chief operating decision maker is considered to be the Bank's Board of Directors.

2. NET INTEREST INCOME

	2012 €m	2011 €m
Interest income and similar income		
Loans and advances to customers	285	224
Amortisation of fair value discount on loans and advances to customers	37	11
Loans and advances to credit institutions	-	1
Total interest income	**322**	**236**
Interest expense and similar charges		
Deposits by credit institutions	(44)	(73)
Debt securities in issue	(76)	(61)
Amortisation of fair value discount on debt securities in issue	(82)	(39)
Acceleration of fair value premium on loans and advances to customers	-	(4)
Total interest expense	**(202)**	**(177)**
Net interest income	**120**	**59**

Included within various captions under interest income for the year ended 31 December 2012 is a total of €33m (2011: €6m) accrued on impaired financial assets.

The acceleration of the fair value premium of €4m is in respect of a premium on mortgage assets purchased from EBS in 2009. The premium was being amortised on an effective interest rate basis, however in 2011 it was deemed appropriate to accelerate the amortisation of the premium and recognise it in full in 2011.

Notes to the accounts

3. NET TRADING EXPENSE

	2012 €m	2011 €m
Interest rate derivative contracts	(10)	(4)

Details on derivative financial instruments are also disclosed in note 17.

4. OTHER OPERATING LOSS

	2012 €m	2011 €m
Gain on repurchase of debt securities in issue	54	-
Loss on the disposal of Loans and advances to customers	(152)	-
	(98)	-

Loss on the disposal of Loans and advances to customers

On 1 October 2012 the Company transferred Loans and advances to customers with a carrying value of €374m to its parent EBS Limited, resulting in a loss on disposal of €152m. The loans and advances to customers were derecognised from the Banks financial statements.

Gain on repurchase of debt securities in issue

During 2012 the following debt securities in issue were bought back by EBS Mortgage Finance.

	2012 April €m	2012 August €m	2012 September €m	**2012 Total €m**
Nominal	150	150	150	**450**
Gain	1	29	24	**54**

Notes to the accounts

5. OPERATING EXPENSES

	2012 €m	2011 €m
Service Fee payable to EBS	7	5
Other expenses	1	1
	8	**6**

Operating expenses includes service fee expense of €7m (2011: €5m) payable to EBS for the period. This fee is in respect of servicing tasks performed by EBS in relation to the portfolio of mortgages sold to the Bank and is determined with reference to the value of the outstanding loans in the Bank.

Directors' remuneration in 2012 is €30k (2011: €30k).

An analysis of the auditor's fees is set out below.

	2012 €m	2011 €m
Fees and expenses paid to our statutory auditors are analysed as follows:		
Audit of the individual financial statements	-	-
Other assurance services	-	-
Other non-audit services	-	-
	-	-

Auditor's remuneration of €12k (2011: €12k) is in relation to the audit of the individual financial statements. No other fees have been paid to the auditors.

The average number of full time persons employed by the Bank in the reporting period was 1.6 (2011: 3.1). All employees are permanent staff members.

Notes to the accounts

6. TAXATION

	2012 €m	2011 €m
Corporation tax charge	-	-
Deferred tax credit	(12)	(10)
	(12)	(10)

The reconciliation of total tax on income at the standard Irish corporation tax rate to the Bank's actual tax charge is analysed as follows:

	2012 €m	2011 €m
(Loss) before tax @ 12.5%	(12)	(10)
Effects of:		
Addbacks and income not taxable at standard rates	-	-
Other temporary differences	-	-
Under/(Over) provision in prior years	-	-
Corporation Tax	(12)	(10)

There was no purchase of group relief from EBS or other subsidiaries of the Group (2011: Nil).

7. LOANS AND ADVANCES TO CREDIT INSTITUTIONS

	2012 €m	2011 €m
Repayable in less than three months	128	130
	128	130

For the purpose of cash flows the cash and cash equivalents comprise the above.

Loans and advances to credit institutions include balances with original maturities of less than 3 months.

Notes to the accounts

8. LOANS AND ADVANCES TO CUSTOMERS

	2012 €m	2011 €m
Repayable on demand	1,067	673
Repayable in less than three months	2	1
Repayable in more than three months but less than one year	3	5
Repayable in more than one but less than five years	93	109
Repayable in more than five years	5,511	6,560
Total customer loans	**6,676**	**7,348**
Less provision for loan impairments	(244)	(171)
Less unearned income provision	(5)	(1)
Total loans and advances to customers after provisions	**6,427**	**7,176**

Loans and advances to customers – Analysis by sector

	2012 €m	2011 €m
Home loans	6,660	6,949
Retail Buy to let loans	16	399
Total loans and advances to customers before provisions	**6,676**	7,348
Less provision for loan impairments	(244)	(171)
Less unearned income provision	(5)	(1)
Total loans and advances to customers after provisions	**6,427**	**7,176**

Fair value of the collateral held for residential mortgages is €5,692m at 31 December 2012 (2011: €6,416m) based on the CSO House Price Index.

Notes to the accounts

PROVISION FOR LOAN IMPAIRMENTS	2012 €m	2011 €m
Individual provision for loan impairments		
At beginning of the period	165	8
Charge of impairment loss	57	17
Impairment provisions utilised	(22)	-
Transfer from collective impairment provision	-	140
At end of period		
At end of period	**200**	**165**
Collective provision for loan impairments		
At beginning of the period	6	34
Charge of impairment loss	43	112
Impairment provisions utilised	(5)	-
Transfer to individual impairment provision	-	(140)
At end of period	**44**	**6**
Total provision for loan impairments at 31 December	**244**	**171**
Unearned income provision	5	1
Total provision for loan impairments (including unearned income provision)	**249**	**172**

The impairment charge recognised in the Income Statement of €94m (2011: €128m) is net of an amount received from EBS of €6m (2011: €1m) as part of an early settlement received by them from Genworth in respect of mortgage indemnity insurance relating to a pool of loans in the Bank.

During 2011, the criteria for determining the individual, and therefore collective provisions were amended. This resulted in €140m of collective provisions being transferred to Individual provisions.

Notes to the accounts

9. INTANGIBLE ASSETS

	2012 €m	2011 €m
Development costs		
At 1 January	3	3
At 31 December	**3**	**3**
Amortisation		
At 1 January	1	1
At 31 December	**1**	**1**
Net book amounts at 31 December	**2**	**2**

Computer software costs are amortised on a straight line basis over a period not exceeding ten years and all are in use at 31 December 2012

10. DEFERRED TAXATION

	2012 €m	2011 €m
At 1 January	10	-
Current tax losses	12	10
At 31 December	**22**	**10**

Comments on the basis of recognition of deferred tax assets on unused tax losses are included in the critical accounting policies.

At 31 December 2012 recognised deferred tax assets on tax losses and other temporary differences totalled €22m (2011: €10m). The tax losses arise in the Irish tax jurisdiction and their utilisation is dependent on the generation of future taxable profits.

11. PREPAYMENTS AND ACCRUED INCOME

	2012 €m	2011 €m
Sundry prepayments	-	1
	-	**1**

Sundry prepayments mainly comprised of up front deferred costs of in respect of the bond issuances which are being amortised over the life of the bonds.

Notes to the accounts

12. DEPOSITS BY CREDIT INSTITUTIONS

	2012 €m	2011 €m
Deposits by credit institutions – Analysis by contractual maturity		
Repayable in less than three months	3,254	3,614

Deposits by Credit Institutions consist of a borrowing facility from the EBS.

The facility limit with EBS is €5bn and the balance at 31 December 2012 amounted to €3.3bn (2011: €3.6bn). The interest rate is equal to the aggregate of Euribor and an applicable margin as agreed from time to time between the Bank and EBS. The facility can be terminated by either the Bank or EBS in accordance with the terms of the loan agreement. The Bank makes repayments under the facility from time to time without any premium, penalty or break costs.

13. DEBT SECURITIES IN ISSUE AND ASSET COVERED SECURITIES ACT INFORMATION

	2012 €m	2011 €m
Mortgage covered securities in issue:		
Opening balance	3,268	2,219
Issued during the year	985	1,010
Redemptions and repayments	(1,312)	-
Gain on repurchase of debt securities in issue	(54)	-
Amortisation of premium / discount	82	40
Closing balance at 31 December	**2,969**	**3,268**
Mortgage covered securities in issue by remaining maturity:		
Repayable in less than one year	497	999
Repayable in more than one year but less than five years	2,472	2,270
	2,969	**3,268**

	2012 €m	2011 €m
Mortgage covered securities in issue - external and internal issuances at nominal value:		
External investors	50	1,050
EBS	3,100	2,550
Nominal value of mortgage covered securities in issue	**3,150**	**3,600**

Notes to the accounts

During 2012 debt securities in issue was bought back by EBS EBS Mortgage Finance, see note 4 for further detail.

During the year ended 31 December 2012 the Bank issued three retained bonds with a total nominal value of €1,000m and these bonds were subscribed in full by EBS. The retained bonds were recognised on the Statement of Financial Position at a value of €985m representing the Day 1 fair value of the bonds as required under the International Financial Reporting Standards. The discount is being amortised through the Income Statement over the life of the bonds.

The Bank is an issuer of mortgage covered securities under the Asset Covered Securities Act, 2001 as amended by the Asset Covered Securities Amendment Act, 2007 (the "Act"). The Act requires that mortgage covered securities are secured by assets that are included in a Cover Assets Pool maintained by the issuer and that a register of mortgage covered securities business is kept.

Section 40(2) of the Act requires that the following information be disclosed in respect of mortgage credit assets that are recorded in the register of mortgage covered securities business.

13 (a) Mortgage properties and principal loan balances outstanding in the cover assets pool

		As at 31 December 2012		As at 31 December 2011	
		Total	Number of	Total	Number of
From €	To €	principal balances €m	loans	principal balances €m	loans
Nil	100,000	972	27,948	1,106	31,536
100,000	200,000	2,021	13,568	2,260	15,143
200,000	500,000	2,598	9,829	3,055	11,450
Over 500,000		188	270	247	344
Total		**5,779**	**51,615**	**6,668**	**58,473**

13(b) Geographical location of related property assets (mortgaged properties) in the cover assets pool

	As at 31 December 2012		As at 31 December 2011	
	Number of mortgaged properties	%	Number of mortgaged properties	%
Geographical area:				
Dublin	14,084	36	15,792	36
Outside Dublin	24,712	64	27,825	64
Total	**38,796**	**100**	**43,617**	**100**

Notes to the accounts

13(c) Non-performing mortgage loans in the cover assets pool
As at 31st December 2012 there were 2,866 (2011: 1,138) accounts in default (the term default is defined as any single loan account where the total amount in arrears is greater than or equal to 3 monthly payments). The total arrears amount for these 2,866 (2011: 1,138) accounts was €5,875,927 (2011: €4,272,827).

13(d) Non-performing mortgage loans in the cover assets pool with arrears greater than €1,000
During the year ended 31 December 2012, 2,627 (2011: 2,139) mortgage loans in the cover assets pool were non performing with arrears greater than €1,000. As at 31 December 2012 834, (2011: 972) mortgage loans were non-performing with arrears greater than €1,000 in the cover assets pool.

13(e) Replacement of non-performing mortgage loan accounts from the cover assets pool
During the year ended 31 December 2012, 1,479 (2011: 1,069) mortgage loan accounts were removed from the Cover Asset Pool. (For this purpose, non-performing is defined as in arrears by six monthly repayments or more). These loan accounts were not replaced with other assets as the Cover Assets Pool continued to meet all regulatory requirements.

13(f) Amount of interest in arrears on mortgage loan accounts in the cover assets pool not written off
Total interest in arrears on mortgage loans in the Cover Asset Pool as at 31 December 2012 was €4,740,845 (2011: €5,466,289). None of the accounts in question were written off as at 31 December 2012.

13(g) Total principal and interest payments on mortgage loan accounts
The total amount of repayments (principal and interest) made by borrowers on mortgage loan accounts in the Cover Assets Pool during the year ended 31 December 2012 was €602.7m (2011: €443.9m), of which €252.5m (2011: €281.4m) represented repayment of principal and €350.2m (€2011: €162.5m) represented payment of interest.

13(h) Number and amount of mortgage loans in the cover assets pool secured on commercial property
As at 31 December 2012 and 2011 there were no loan accounts in the Cover Asset Pool that were secured on commercial properties.

14. ACCRUALS AND DEFERRED INCOME

	2012 €m	2011 €m
Interest payable on mortgage covered securities	1	5
Other accruals	1	1
At 31 December	**2**	**6**

15. OTHER LIABILITIES

	2012 €m	**2011 €m**
Funding liabilities fair value hedge	-	2

Other liabilities in 2011 consist of the fair value adjustment to the carrying value of €1bn debt securities in a fair value hedge relationship of €2m, during 2012 the hedged items (swap and bond) matured.

Notes to the accounts

16. EMPLOYEE BENEFITS

The Bank is a participating employer in the EBS pension plan. The Bank participates in a defined benefit and a defined contribution pension scheme. The defined benefit scheme is based on final pensionable pay and operated for eligible employees of EBS and the Bank. Whilst the scheme is a defined benefit scheme, the Bank is unable to identify its share of the underlying assets and liabilities of the scheme on a consistent and reasonable basis, hence it is treated as a defined contribution scheme in the accounts of the Bank.

The cost of the defined contribution pension scheme is charged to the income statement in the accounting period in which it is incurred. Any contributions unpaid at the reporting date are included as a liability. The Bank has no further obligation under this scheme once these contributions have been paid.

Contributions on behalf of the Bank employees amounted to €15k (2011: €29k).

17. DERIVATIVE FINANCIAL INSTRUMENTS

EBS Mortgage Finance

Group operations are exposed to the risk of interest rate fluctuations to the extent that assets and liabilities re-price at different times or in differing amounts. Derivatives allow the Bank to modify the re-pricing characteristics (including resetting mortgage asset swap margins by agreement of both couterparties) of assets and liabilities in a cost efficient manner. This flexibility helps the Bank to achieve liquidity and risk management objectives.

Derivatives fluctuate in value as interest rates rise or fall just as all other assets and liabilities fluctuate in value. If the derivatives are purchased or sold as hedges of balance sheet items, the appreciation or depreciation of the derivatives, as interest or exchange rates change, will generally be offset by the unrealised appreciation or depreciation of the hedged items.

To achieve its risk management objectives, the Bank uses interest rate swaps. The Bank only engages in derivative activity for hedging purposes, although all swaps are considered to be effective hedges in economic terms, due to the nature of some it is not possible to establish a "Fair Value" hedging relationships under IAS 39, such swaps are classified as "Fair Value through the Income Statement".

Derivative instruments are contractual agreements whose value is derived from the price movements in underlying assets, interest rates or indices. Derivatives are an efficient and cost effective means of managing market risk and limiting counterparty exposure.

The Bank hedges part of its existing interest rate risk resulting from any potential movement in the fair value of fixed rate assets or liabilities using interest rate swaps. The net fair value of these swaps at 31 December 2012 was (€1m) (2011: €1m).

Notes to the accounts

	2012			2011		
	Notional principal amount	*Assets*	*Liabilities*	*Notional principal amount*	*Assets*	*Liabilities*
	€m	*€m*	*€m*	*€m*	*€m*	*€m*
Derivatives held for trading						
Interest rate swaps	6,963	35	36	7,726	55	54
Total trading contracts	**6,963**	**35**	**36**	**7,726**	**55**	**54**
Derivatives designated as fair value hedges						
Interest rate swaps	-	-	-	1,000	1	-
Total hedging contracts	**-**	**-**	**-**	**1,000**	**1**	**-**
Total derivative financial instruments	**6,963**	**35**	**36**	**8,726**	**56**	**54**

Derivative assets of €35m (2011: €56m) and derivative liabilities of €36m (2011: €54m) represent fair value of the derivative and accrued interest on them. Accrued interest receivable on all derivatives is included in derivative assets. Similarly, accrued interest payable in respect of all derivatives is included in derivative liabilities.

Fair value is based upon quoted market prices where available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar instruments and adjusted for differences between the quoted instrument and the instrument being valued. In certain cases, including some loans and advances to customers, where there are no ready markets, various techniques using observable data have been used to estimate the fair value of the instruments. These estimates are subjective in nature and involve uncertainties and matters of significant judgement and therefore can not be determined with precision. Readers of these financial statements are advised to use caution when using the data to evaluate the Bank's financial position or to make comparisons with other institutions.

Notes to the accounts

The derivative maturity table below analyses the asset, liability and embedded derivatives notional amounts by maturity bucket.

Derivative Maturity Table – at 31 December 2012

	Not more than 12 months €m	Over 1 year but not more than 5 years €m	Over 5 years €m	Total €m
Interest Rate Swaps	-	5,657	1,306	6,963
Total	**-**	**5,657**	**1,306**	**6,963**

The methods and assumptions used in determining fair value are described in the Risk Management Report.

Derivative Maturity Table – at 31 December 2011

	Not more than 12 months €m	Over 1 year but not more than 5 years €m	Over 5 years €m	Total €m
Interest Rate Swaps	1,000	6,301	1,425	8,726
Total	**1,000**	**6,301**	**1,425**	**8,726**

Notes to the accounts

The derivative maturity table below represents the Positive fair value of interest rate swaps on asset derivatives based on yield curves as at 31 December 2012:

Positive fair value of interest rate swaps table – at 31 December 2012

	Not more than 12 months €m	Over 1 year but not more than 5 years €m	Over 5 years €m	Total €m
Interest Rate Swaps	-	22	13	35
Total Assets	-	22	13	35

Positive fair value of interest rate swaps table – at 31 December 2011

	Not more than 12 months €m	Over 1 year but not more than 5 years €m	Over 5 years €m	Total €m
Interest Rate Swaps	7	30	19	56
Total Assets	7	30	19	56

18. RELATED PARTY TRANSACTIONS

The immediate holding company and controlling party is EBS Limited, with a registered office at 2 Burlington Road, Dublin 4. The ultimate holding entity and controlling party is Allied Irish Banks, p.l.c, with a registered office at Bankcentre, Ballsbridge, Dublin 4. Copies of both EBS Group and AIB Group financial statements are available from the registered office of Allied Irish Banks, p.l.c. The only related party transactions are normal banking transfers to and from EBS.

The Irish Government and Government related entities
The Irish Government has taken a range of measures to stabilise the Irish banking system since the commencement of the financial crisis in 2008. These measures have included the injection of equity and preference share capital into Allied Irish Banks, p.l.c As a result of these capital injections, the Irish Government, through the NPRFC, now holds 99.8% of the ordinary shares of Allied Irish Banks, p.l.c and €3.5bn in 2009 Preference Shares. In addition, the Minister for Finance holds €1.6bn of contingent capital notes.

Notes to the accounts

As a result of the various measures taken by the Irish Government (specifically the guarantee schemes, the Direction Order, and the capital injections) the Irish Government is a related party to Allied Irish Banks, p.l.c and therefore EBS Mortgage Finance. Details regarding these measures, as well as others taken in the context of the Irish banking crisis, are set out below.
The Minister for Finance (the 'Minister') and/or the Central Bank of Ireland has considerable rights and powers over the operations of the AIB Group (and other financial institutions) arising from the various stabilisation measures.

These rights and powers include, inter alia:

- The acquisition of shares in other institutions;
- Maintenance of solvency ratios and compliance with any liquidity and capital ratios that the Central Bank, following consultation with the Minister, may direct;
- The appointment of non-executive directors and board changes;
- The appointment of persons to attend meetings of various committees;
- Restructuring of executive management responsibilities, strengthening of management capacity and improvement of governance;
- Declaration of payment dividends;
- Restrictions on various types of remuneration;
- Buy-backs or redemption of its shares;
- The manner in which EBS extends credit to certain customer groups; and
- Conditions regulating the commercial conduct of Allied Irish Banks, p.l.c, having regard to capital ratios, market share and the EBS' balance sheet growth.

(a) Irish Government Guarantee Schemes:
The Bank is a covered institution under the Government's Credit Institutions (Finance Support) Scheme 2008 (the 'CIFS Scheme') which guaranteed covered liabilities raised by covered institutions up to 29 September 2010. Covered liabilities that were covered by the CIFS Scheme were those liabilities in respect of retail and corporate deposits (to the extent not covered by existing deposit protection scheme in Ireland or any other jurisdiction), inter-bank deposits and senior unsecured debt excluding any intra group borrowing and any debt due to the European Central Bank arising from Eurosystem monetary operations. Under the terms of the CIFS Scheme the Central Bank in consultation with the Minister regulated the commercial conduct of covered institutions strictly in order to achieve the objectives of this scheme.

(b) National Asset Management Agency (NAMA)
The Irish Government set up an asset relief scheme in 2009 under the auspices of the National Asset Management Agency in Ireland. The Bank is a participating institution in NAMA. However, no loans were transferred from the Bank to NAMA.

(c) Credit Institutions (Stabilisation) Act 2010
The Credit Institutions (Stabilisation) Act 2010 was passed into Irish law on 21 December 2010. The Act provides the legislative basis for the reorganisation and restructuring of the Irish banking system agreed in the joint EU/IMF Programme for Ireland ('the Programme'). This will allow the Minister for Finance ("the Minister") to take the actions required to bring about a domestic retail banking system that is proportionate to and focused on the Irish economy.

The Act provides broad powers to the Minister (in consultation with the Governor of the Central Bank of Ireland) to act on financial stability grounds to effect the restructuring actions and recapitalisation measures envisaged in the Programme. The Act applies to banks which have received financial support from the State, building societies and credit unions. Given the exceptional nature of the powers contained in the Act, the powers are time-limited and were scheduled to expire on 31 December 2012. However, in January 2013, the Minister extended the period of effectiveness of the Act for a further period of two years until 31 December 2014.

Notes to the accounts

The powers provided in the Act allow the Minister to implement key aspects of the agreed Programme for bank restructuring and include the issue of direction orders, special management orders, subordinated liabilities orders and transfer of assets and liabilities orders. In addition, the Act gives the Minister broad powers in relation to directors and officers and their appointment/removal/duties. Various other terms are also imposed on relevant financial institutions as a condition for financial support.

(d) Central Bank and Credit Institutions (Resolution) Act 2011
The Central Bank and Credit Institutions (Resolution) Act 2011 was signed into law on 20 October 2011 and became effective on 28 October 2011.

This legislation provides the Central Bank with additional powers to achieve an effective and efficient resolution regime for credit institutions that are failing or likely to fail and that is effective in protecting the Exchequer and the stability of the financial system and the economy.

The Act give the Central Bank power to take control of banks, appoint managers to run them and remove directors, staff and consultants and to move their deposits and loans to other banks. It provides for the establishment of a Credit Institution Resolution Fund which would provide a source of funding for the resolution of financial instability or in the event of an imminent serious threat to the financial stability of an authorised credit institution. Authorised credit institutions will be obliged to contribute to the resolution fund.

The Act provides for the establishment of "Bridge-Banks" for the purpose of holding assets or liabilities which have been transferred under a transfer order. Bridge-Banks are only intended to hold such assets or liabilities on a temporary basis pending onward transfer as soon as possible.

The Central Bank will also be empowered to make special management orders in relation to an authorised credit institution or in relation to a subsidiary or holding company of the authorised credit institution in certain circumstances. The Act also provides powers to the Central Bank regarding the liquidation of authorised credit institutions. Authorised credit institutions may also be directed to prepare a recovery plan setting out actions that could be taken to facilitate the continuation or secure the business or part of the business of that institution.

The legislation is expected to, in due course, replace the provisions of the Credit Institutions (Stabilisation) Act 2010 outlined above which ceases to have effect on 31 December 2014 or at a later date substituted by resolution of both Houses of the Oireachtas.

(e) Government related entities
As a result of the capital received from Government in 2010 and the participation in the Government guarantee scheme, the Government is recognised as a related party, as defined under the accounting standards.
In the normal course of business the Group has transactions with the Government, state departments and semi-state bodies and state owned financial institutions including the holding of securities issued by the Government and semi-state bodies.

(f) Transactions with immediate parent
The following amounts represent the transactions and outstanding balances with the EBS:

- Loans from related parties at 31 December 2012 are €3,254m (2011: €3,614m).
- Deposits with related parties at 31 December 2012 are €58m (2011:€ 17m).
- The nominal value of debt securities in issue to related parties at 31 December 2012 are €3,100m (2011:€ 2,550m).

Notes to the accounts

Derivative financial instruments with the parent company (EBS Limited)

Interest rate swaps	2012 €m	2011 €m
Notional Principal amount	6,913	7,676
Assets (Fair value)	35	55
Liabilities (Fair value)	35	54

At 31 December 2012 there were no transactions between the Bank and the ultimate Parent, Allied Irish Banks, p.l.c

	2012 €m	2011 €m
Income and expense included in the Income Statement from related parties:		
Service fee	(7)	(5)
Interest expense on loans	(44)	(73)
Interest income from deposits	-	1
Gain on repurchase of debt securities in issue (see note 4)	54	-
Interest expense on debt securities	(122)	(58)
Net trading income	(10)	(4)

The above transactions arose in the ordinary course of business. The interest charged and interest earned involving related parties is at normal commercial rates appropriate to the transaction.

There have been no contracts or arrangements with the Bank in which a director of the Bank was materially interested and which were significant in relation to the Bank's business.

Transactions with key management personnel

For the purpose of IAS 24: Related Party Transactions, 'key management personnel' comprises executive and non executive directors.

Loans to key management personnel are made in the ordinary course of business and on normal commercial terms. Loans are made (i) by the parent company on terms applicable to other employees of the parent company, in accordance with established policy, within limits set on a case by case basis, and/or (ii) otherwise, on normal commercial terms.

	2012 €m	2011 €m
At 31 December : Loans outstanding	0.2	1.2

The loans outstanding were to 1 director (2011: 2 Directors).

Non executive directors are compensated by way of fees. Details of the compensation of non executive directors are set out in note 5 'Operating Expenses'. Executive directors' emoluments for the period were Nil (2011: nil).

Notes to the accounts

19. CAPITAL MANAGEMENT

From 1 January 2008 the minimum regulatory capital requirement of the Bank's operations has been calculated in accordance with the provisions of Basel II as implemented by the European Capital Requirements Directive and the Irish Central Bank. The objective of Basel II is to more closely align bank regulatory capital with the economic capital required to support the risks being undertaken. The capital required to cover credit, operational and market risks is required to be explicitly measured under the Basel II methodology. In implementing Basel II, the Bank has adopted the standardised approach to credit risk.

The Bank sets and monitors capital policy in line with regulatory and legislative requirements. Capital adequacy is monitored by the Executive Management Team.

The Bank is required under the terms of its banking license to maintain a solvency ratio of at least 9%. EBS Mortgage Finance maintained at least this ratio throughout 2012. No increase in the minimum capital requirement has been requested by the Central Bank for the Bank.

The Bank's regulatory capital comprises:

Tier 1 capital, which includes ordinary share capital, general reserve capital, deductions for intangible assets. Tier 2 capital is comprised of collective impairment provision add back.
Within these tiers, limits are set for different components of capital. Qualifying Tier 2 capital cannot exceed Tier 1 capital. There also are restrictions on the amount of collective impairment allowances that may be included as part of Tier 2 capital.

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

The Bank's policy is to ensure that sufficient capital is in place to meet regulatory requirements.

The Bank's regulatory capital position at 31 December was as follows:

	2012 €m	2011 €m
Tier 1 capital		
Ordinary Share Capital	477	477
Profit and loss account	(124)	(46)
Intangible assets	(2)	(2)
Total	**351**	**429**
Tier 2 capital		
Collective allowances for impairment	44	8
Total regulatory capital	395	437

Notes to the accounts

20. SHARE CAPITAL	2012 €m	2011 €m
Authorised:		
1,000,000,000 ordinary shares of €1.00 each	1,000	1,000
Issued and fully paid:		
476,540,000 ordinary shares of €1.00 each	477	477
(2011: 476,540,000 ordinary shares of €1.00 each)		

On 21 December 2011, the Bank issued 160,000,000 €1 ordinary shares to EBS.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the bank. All shares rank equally with regard to the bank's residual assets.

21. REGULATORY COMPLIANCE

During December 2011, EBS Mortgage Finance breached the large exposures limit. This arose due to the acquisition of loans from EBS in November 2011. The issue was resolved and the exposures were brought back within limits in January 2012. There were no other issues in 2012.

22. EVENTS SINCE THE REPORTING DATE

In January 2013 EBS launched a voluntary severance programme which is expected to be available to all staff. EBS retains responsibility for the delivery to EBSMF of its' obligations under the Master Service Agreement not withstanding any reduction in staffing levels in EBS.

In the directors' view, there have been no events since the year end that have had a material effect on the financial position of the Bank.

23. APPROVAL OF FINANCIAL STATEMENTS

The financial statements were approved by the board of directors on the 26 March 2013.