



Annual Report 2011.



INTESA SANPAOLO BANKA

Bosna i Hercegovina

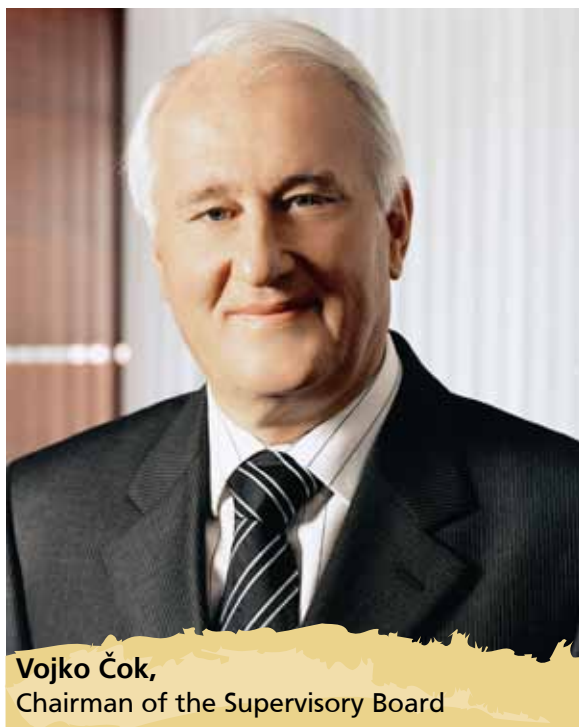
Intesa Sanpaolo Banka d.d. BiH

FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011
AND INDEPENDENT AUDITORS' REPORT

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Report on Supervisory Board activities



Vojko Čok,
Chairman of the Supervisory Board

During the year 2011, the Supervisory Board of Intesa Sanpaolo Banka d.d. Bosna i Hercegovina (hereinafter: "the Bank") held 7 meetings on the following dates: 23.02.; 28.04.; 01.06.; 28.07.; 26.10.; 14.12 and 23.12.2011, which were recorded under sequential numbers from 38 to 44.

The Supervisory Board of the Bank carried out its activities in accordance with the Charter of the Bank and along with significant support by the Management Board and Audit Committee.

At the meetings held, the Bank's Supervisory Board considered, analyzed and discussed various general and internal acts of the Bank, including policies and procedures, prepared internally but also those Group ones from the Parent Company. The Supervisory Board put particular efforts and attention to analyzing and discussing Bank's financial reports and followed up internal and external auditors' activities, during the year.

Among the major issues and topics that the Supervisory Board discussed are results of Stress Test on Capital Adequacy ratio, both official and unofficial. Supervisory Board will continue to follow up with this issue, staying committed in respecting the local regulation about the capital adequacy ratio and advising Management Board on further actions.

The Supervisory Board also paid special attention to AML activities and reports, provided by the Compliance and AML Department.

As per local regulatory requirement, Supervisory Board also received and considered all information related to BCM and tests performed as well as to local regulatory requirements referring to reports on written complaints that the Bank received. The Supervisory Board assessed these Bank's activities successful.

The Supervisory Board also supported Bank's Management Board in adopting and implementing internal methodology for measurement of the impairment in loans and other financial assets according to the IAS and IFRS.

Through adoption of Operational Reports, Report of independent External Auditors the Supervisory Board of the Bank acknowledged work of the Management Board, assessing it as successful and compliant with laws, internal acts, decisions, policies, procedures and programs.

Significant involvement of the Supervisory Board of Intesa Sanpaolo Banka d.d. Bosna i Hercegovina in all Bank's activities contributed to stability and maintenance a good position of the Bank in the market, thus, achieving good financial results.

As far as composition of the Supervisory Board is concerned, the members of the Supervisory Board of Intesa Sanpaolo Banka d.d. Bosna i Hercegovina, during 2011 were: **Mr. V. Čok** (Chairman), **Mr. Massimo Pierdicchi** (Deputy Chairman), **Ms. Beata Kissne Foldi**, **Mr. Luca Finazzi** and **Ms. Nora Kocsis**. Due to resignation of Ms. Nora Kocsis to the membership in the Supervisory Board, at the General Shareholders Meeting of the Bank, held on July 20, 2011, Ms. Nora Kocsis was replaced by **Mr. Ivan Sramko** as Deputy Chairman of the Board while **Mr. Massimo Pierdicchi** was appointed member of the Board. Starting from statements presented in this Report, the Supervisory Board proposes to the Bank's General Shareholder's Meeting the following:

- Decision on Accepting Report on the Operation of the Bank for period 01.01.-31.12.2011. along with the Report of the External and Internal Auditor, Supervisory Board Report, Audit Committee Report and Basics of Business Plan for 2012 of Intesa Sanpaolo Banka d.d. Bosna i Hercegovina;
- Decision on adoption of Annual Statements of Accounts for the period 01.01. – 31.12.2011;
- Decision on Distribution of the Profit for 2011 of the Intesa Sanpaolo Banka d.d. Bosna i Hercegovina;

Chairman of the Supervisory Board
Vojko Čok

Management Board Report on Bank's Operations



Almir Krkalić,
CEO

In accordance with Article 40 of the Law on Accounting ("FBiH Official Gazette" no. 83/2009), Management Board of Intesa Sanpaolo Banka d.d. BiH presents business results of the Bank for 2011.

Intesa Sanpaolo Banka d.d. BiH continued the good performance recorded already in previous years, despite the consequences of the financial crisis that still affect the economy worldwide and in BH in particular. The Bank managed to increase its market share in credit financing and maintained strong control upon worsening of non-performing portfolio, especially in retail segment where the Bank significantly outperformed the banking sector, while also in corporate segment the quota of NPLs with respect to the total portfolio remains much lower than the sector's level. Like in previous years, this result was due to well-structured credit lending approval and subsequent monitoring procedures, together with a close cooperation with clients in designing appropriate and sustainable business development and reimbursement plans

The following are the major indicators evidencing the quality of the Bank's operations.

In 2011 and in comparison to the past year, the Bank accomplished net profit in the amount of

10,308 thousand KM, which is higher for 70.1 %, the assets increased for 2.82 % and reached the amount of 1.341 million KM, total deposits amounted to 822 mil KM and they are at the same level as in 2010, the loan portfolio recorded a growth of 12.3 % reaching the amount of 1,094 mil KM.

Despite the still not favourable market conditions the Bank proceeded with its lending activities, increasing the total loan portfolio by 12.3 % in comparison with previous year. Notwithstanding the unfavourable macro-economic conditions and the still significant unemployment rate, Retail segment recorded a positive recovery after the negative trend of 2010, with an increase in issued loans by 8%. On the other hand, corporate segment started suffering the impact of the crisis and grew less than in 2010. This did not prevent the Bank from recording anyway a double-digit growth of gross corporate exposures, at 15.54.

As for liquidity management, the Bank timely negotiated funding sources with the parent company and international organizations, thus minimizing the impact of fluctuating cost of funds while, at the same time, granting permanent funds' availability to customers in needs of financing.

During 2011, the European Bank for Reconstruction and Development sold its participation in the Bank, which was entirely taken over by the parent company, thus confirming once again the commitment of Intesa Sanpaolo Group to strengthen its presence in Bosnia Herzegovina and strongly support the Bank's operations in the country. Incidentally, the capital adequacy ratio of the Bank remained above the minimum requirements, despite the mentioned growth of the business. In this perspective, the Bank is planning a capital increase once again evidencing its focus on further future growth, while complying with regulators' requirements and shareholders and customers expectations.

The commercial presence of the Bank on Bosnia Herzegovina market and our attention for customers' needs is emphasized by the opening of one additional agency and further expansion of ATM and POS network. At the same time, the Bank proceeded in distributing on the market new financial products, supported by

more efficient tools and unique characteristics (like the ISP Group debit card).

Like in past years, focus on customers means for our Bank also promptness in providing feedbacks in case of complaints or requests for clarifications and constant monitoring of customers' satisfaction through advanced surveying tools. In this area, we proudly keep on recording the leading position on the Bosnian market in terms of European Customer Satisfaction Index, with distinctive top rates as far as company's Image, After Sale care of customers and Relationship with Personnel and Branch Organization.

Customer care is not separate, for Intesa Sanpaolo Banka d.d. BiH, from social responsibility, which also in 2011 resulted in direct support to social activities and in particular in support for students' scholarship and special awarding programs for universities' students, together with cooperation with several no-profit organizations.

At the same time, in a period of difficulties for countrymen in finding or keeping their jobs, the Bank managed to develop further its workforce and strengthened its programs for employees permanent training, also through the full implementation of modern training tools like "distance learning", that enable a timely circulation of information on new regulations, new products and methodologies.

Main objectives of the Management Board of the Bank and its staff in the following period are:

Further Sustainable Growth of Loans Portfolio, through

- ✎ Acquisition of stable small&medium businesses and large corporate clients through quality Bank's products and services.
- ✎ Maintaining competitive prices leveraging upon most convenient "purpose" credit lines from international organizations.
- ✎ More aggressive approach of active communication flows with existing and new clients, together with retail division, in order to cross sell bank's products and services.
- ✎ Special offers promotion through specific selling actions.
- ✎ Further simplification of issuing process for existing loan products.
- ✎ Development of alternative distribution channels

Strict Monitoring of Credit Assets Quality, through

- ✎ Internal corporate rating implementation: Development and management of corporate portfolio based on internal rating.
- ✎ Optimization of portfolio based on the risk/return profile.
- ✎ Improvement of collateral monitoring by further developing dedicated IT applications and collaterals-related procedures.

Strict Monitoring on Operational Costs, through selected capital investments specifically aimed at supporting business developments and rationalization of standard operational expenses, also based on new procurement policies and procedures.

Human Resources enhancement, through

- ✎ Continuous training of all resources through distance learning tools recently implemented.
- ✎ Leveraging Group training programs both for technical topics and for development of managerial skills (e.g. Leadership program)

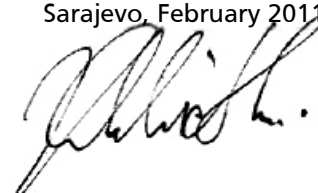
Network optimization, through

- ✎ Opening of 1 new branch in a country area not yet covered.
- ✎ Further renovation of selected branches according to Group standards.
- ✎ Further penetration in merchants' network through POSs and leveraging on successful new Inspire Debit Card.

In addition, detailed explanation of the policy of the Bank in reference to financial risks management, exposure of the Bank to the price risk, FX risk, credit risk, capital and liquidity risks can be found in details in the notes 32 and 33 of the Financial Statements of the Bank for 2011, audited by external auditor REVSAR.

Almir Krkalić, CEO

Sarajevo, February 2011



Responsibility for the Financial Statements

Pursuant to the Law on Accounting and Audit of Federation of Bosnia and Herzegovina (Official Gazette No. 83/2009), the Management Board is responsible for ensuring that financial statements are prepared for each financial year in accordance with accounting regulations applicable to financial reporting of banks in the Federation of Bosnia & Herzegovina, which give a true and fair view of the state of affairs and results of the IntesaSanpaolo Banka Bosna and Hercegovina d.d. for that period.

After making enquiries, the Management Board has a reasonable expectation that the Bank has adequate resources to continue in operational existence for the foreseeable future. For this reason, the Management Board continues to adopt the going concern basis in preparing the financial statements.

In preparing those financial statements, the responsibilities of the Management Board include ensuring that:

- suitable accounting policies are selected and then applied consistently;
- judgments and estimates are reasonable and prudent;
- applicable accounting standards are followed, subject to any material departures disclosed and explained in the financial statements; and
- the financial statements are prepared on the going concern basis unless it is inappropriate to presume that the Bank will continue in business.

The Management Board is responsible for keeping proper accounting records, which disclose with reasonable accuracy at any time the financial position of the Bank and must also; ensure that the financial statements comply with the Accounting and Auditing Law of Federation of Bosnia and Herzegovina. The Management Board is also responsible for safeguarding the assets of the Bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Signed on behalf of the Management Board



Almir Krkalić, Director
Intesa Sanpaolo Banka d.d. Bosna i
Hercegovina
Obala Kulina bana 9a
71000 Sarajevo
Bosnia and Herzegovina

22. February 2012

Revsar d.o.o., Sarajevo

Independent auditors' report

**TO THE SHAREHOLDERS OF INTESA
SANPAOLO BANKA D.D. BOSNA I
HERCEGOVINA**

We have audited the accompanying financial statements of IntesaSanpaolo Banka d.d. BosnaiHercegovina (hereinafter: the Bank), which comprise the balance sheet as at 31 December 2011, and the income statement, statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting regulations applicable to financial reporting of banks in the Federation of Bosnia & Herzegovina, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether

the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Bank as at 31 December 2011, and of its financial performance and its cash flows for the year then ended in accordance with accounting regulations applicable to financial reporting of banks in the Federation of Bosnia & Herzegovina.

Alma Delić, Certified auditor,
licence number 3090143102

Hajrudin Hadžović, Certified auditor,
licence number 3090262100



Remzija Bejtović,
Director

Sarajevo, 22 February, 2012

INTESA SANPAOLO BANKA, D.D. BIH
STATEMENT OF INCOME FOR THE YEAR ENDED 31 DECEMBER 2011
(all amounts are expressed in thousands of KM)

	Notes	2011	2010
Interest income	5	78,314	71,642
Interest expense	6	(23,872)	(22,015)
Net interest income		54,442	49,627
Fee and commission income	7	14,397	12,396
Fee and commission expense	8	(3,570)	(3,275)
Net fee and commission income		10,827	9,121
Net foreign exchange income	9	1,309	1,467
Other operating income	10	436	909
Operating income		1,745	2,376
Personnel expenses	11	(19,288)	(18,260)
Administrative expenses	12	(17,970)	(17,253)
Depreciation of fixed assets	23	(4,822)	(4,902)
Operating Expense		(42,080)	(40,415)
PROFIT BEFORE IMPAIRMENT LOSSES, PROVISIONS AND INCOME TAX		24,934	20,709
Impairment losses and provisions	13	(13,419)	(18,508)
Recoveries of written off loans	14	-	4,743
PROFIT BEFORE INCOME TAX		11,515	6,944
Income tax	15	(1,207)	(883)
NET PROFIT FOR THE YEAR		10,308	6,061
Earnings per share (KM)	16	23,03	13,47

The accompanying notes form an integral part of these financial statements.

Approved by and signed on behalf of IntesaSanpaolo Banka d.d. BosnaiHercegovina
On 22February 2012:


Almir Krkalic
Director


Dario Grassani
Executive Director of Finance

INTESA SANPAOLO BANKA, D.D. BIH
STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2011
(all amounts are expressed in thousands of KM)

	<u>2011</u>	<u>2010</u>
Profit for the year	10,308	6,061
Other comprehensive income for the year		
Net gains/(losses) on financial assets available for sale:		
Gains arising during the year	33	93
Losses during the year	-	(18)
Reclassification adjustments for gains included in the statement of income	(7)	(87)
Income tax relating to items of other comprehensive income	<u>(1)</u>	<u>(1)</u>
Total comprehensive income for the year, net of tax	<u>10,333</u>	<u>6,048</u>

The accompanying notes form an integral part of these financial statements.

Approved by and signed on behalf of IntesaSanpaolo Banka d.d. BosnaiHercegovina
 On 22February 2012:



 Almir Krkalic
 Director



 Dario Grassani
 Executive Director of Finance

INTESA SANPAOLO BANKA, D.D. BIH
STATEMENT OF FINANCIAL POSITION AT 31 DECEMBER 2011
(all amounts are expressed in thousands of KM)

	Notes	31 December 2011	31 December 2010 restated
ASSETS			
Cash and cash equivalents	17	163,791	66,364
Obligatory reserve with the Central Bank	18	71,158	97,789
Placements with other banks	19	31,520	190,264
Loans and receivables	20	1,018,609	907,798
Assets available for sale	21	15,933	979
Other assets	22	9,040	9,238
Property, plant and equipment	23	25,425	25,604
TOTAL ASSETS		1,335,476	1,298,036
LIABILITIES			
Due to banks and other institutions	24	441,942	449,297
Subordinated debt	25	1,083	1,244
Due to customers	26	719,409	689,597
Other liabilities	27	10,252	6,826
Other provisions	28	2,639	2,299
Provisions for contingent liabilities and commitments	29	2,341	1,296
TOTAL LIABILITIES		1,177,666	1,150,559
SHAREHOLDERS' EQUITY			
Share capital		44,782	44,782
Reserves and retained earnings		113,028	102,695
TOTAL SHAREHOLDER'S EQUITY		157,810	147,477
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		1,335,476	1,298,036
FINANCIAL COMMITMENTS AND CONTINGENCIES	29	176,809	127,149

The accompanying notes form an integral part of these financial statements.

Approved by and signed on behalf of IntesaSanpaolo Banka d.d. Bosnai Hercegovina
On 22 February 2012:


Almir Krkalic
Director



Dario Grassani
Executive Director of Finance

INTESA SANPAOLO BANKA, D.D. BIH
STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2011
(all amounts are expressed in thousands of KM)

	2011	2010
Operating activities		
Net Income	10,308	6,061
<i>Adjustments to reconcile net income to net cash provided by operating activities:</i>		
Depreciation and amortization	4,822	4,902
Impairment losses and provisions	13,419	18,508
Changes in other provisions, net	-	293
(Gain) on sale or disposal of property, plant and equipment	20	(62)
<i>Changes in operating assets and liabilities:</i>		
Net (increase)/decrease in due from Central Bank	26,631	(9,017)
Net (increase)/decrease in placements with other banks, before impairment losses	158,762	(55,588)
Net (increase)/decrease in loans and receivables, before impairment losses	(124,003)	(109,546)
Net (increase)/decrease in other assets, before impairment losses	459	(1,419)
Net (decrease)/increase due to banks	(30,036)	21,902
Net increase in demand and term deposits	29,814	26,854
Net (decrease)/increase in other liabilities	3,765	(451)
NET CASH FROM/(USED IN) OPERATING ACTIVITIES	93,961	(97,563)
Investing Activities		
Net increase in assets available for sale, before impairment losses	(14,111)	(459)
Net purchases of property and equipment	(3,455)	(2,414)
Proceeds from sale of property, plant and equipment	(1,486)	330
NET CASH USED IN INVESTING ACTIVITIES	(19,052)	(2,543)
Financing Activities		
Net proceeds from borrowings	22,681	66,125
Net repayments of subordinated debt	(163)	(158)
NET CASH PROVIDED BY FINANCING ACTIVITIES	22,518	65,967
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS	97,427	(34,139)
CASH AND CASH EQUIVALENTS AT 1 JANUARY	66,364	100,503
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	163,791	66,364
Operational cash flow from interest and dividends		
Interest paid	24,121	24,045
Interest received	72,850	67,357
Dividend received	35	-

The accompanying notes form an integral part of these financial statements.

Approved by and signed on behalf of IntesaSanpaolo Banka d.d. BosnaiHercegovina
On 22 February 2012:


Almir Krkalic
Director


Dario Grassani
Executive Director of Finance

INTESA SANPAOLO BANKA, D.D. BIH
STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY FOR THE YEAR ENDED 31 DECEMBER 2011
(all amounts are expressed in thousands of KM)

	Share capital	Treasury shares	Share Premium	Fair Value reserves	Retained earnings and reserves	Total
Balance as at 31 December 2009	45,296	(514)	57,415	6	20,947	123,150
Total comprehensive income	-	-	-	(13)	6,061	6,048
Purchase/Sale of treasury shares	(514)	514	-	-	-	-
Balance as at 31 December 2010	44,782	-	57,415	(7)	27,008	129,198
Balance as at 31 December 2010 Before restatement	44,782	-	57,415	(7)	27,008	129,198
Restatement *					18,279	18,279
Balance as at 31 December 2010 after restatement	44,782	-	57,415	(7)	45,287	147,477
Total comprehensive income	-	-	-	25	10,308	10,333
Balance as at 31 December 2011	44,782	-	57,415	18	55,595	157,810

*Restatement is effect of adoption of new accounting policies for impairment of financial assets and provisions for contingent liabilities.

The accompanying notes form an integral part of these financial statements.

Approved by and signed on behalf of IntesaSanpaolo Banka d.d. Bosna i Hercegovina
On 22 February 2012:


Almir Krkalic
Director


Dario Grassani
Executive Director of Finance

INTESA SANPAOLO BANKA, D.D. BIH
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011
(all amounts are expressed in thousands of KM)

1. GENERAL

History and incorporation

IntesaSanpaoloBanka d.d. Bosna i Hercegovina, former UPI banka d.d. Sarajevo, Obala Kulina Bana 9a (the "Bank") is registered in the Cantonal Court in Sarajevo on 20 October 2000.

The Bank was established in 1972 as an internal bank of the corporate system of the Udruženje poljoprivredna, prehrambena i industrija i promet (Associated Agriculture and Food Industries and Sales), aimed at supporting the operations of these sectors, which at the time employed more than 35,000 workers. Since 1990, a new phase is coming in the development of the Bank, when it was registered as a shareholding company and it is in a majority state ownership (92 %). The Bank starts with expansion of the network of corporate clients, focusing on the sector of small and medium entrepreneurship. As early as from the year 2000, through the emission of shares, the Bank was fully transferred into the hand of private capital.

In February 2006, IntesaSanpaolo Holding International S.A. took over the major share package of UPI Banka d.d. Sarajevo, and became the major owner of the Bank's shares.

On 31 July 2007, LT Gospodarska banka d.d. Sarajevo (the "LTG Bank"), also subsidiary of IntesaSanpaolo Holding, merged into the Bank, with the effect of the LTG Bank cancellation (without initiation of liquidation process), while the Bank became its legal successor.

On 20 August 2008 the Bank changed its name into IntesaSanpaolo Banka d.d. Bosna i Hercegovina.

Principal activities of the Bank

The Bank's main operations are as follows:

1. Accepting deposits from the public and placing of deposits,
2. Providing current and term deposit accounts,
3. Granting short-term and long-term loans and guarantees to corporate customers, private individuals, local municipalities and other credit institutions dealing with finance lease and foreign exchange transactions,
4. Money market activities,
5. Performing local and international payments,
6. Foreign currency exchange and other banking-related activities,
7. Providing banking services through an extensive branch network in Bosnia and Herzegovina

Supervisory Board

Vojko Čok	Chairman
Massimo Pierdicchi	Vice-Chairman until July 20, 2011 and Member from July 21, 2011
Ivan Sramko	Vice-Chairman from July 21, 2011
Beata Kissné Foldi	Member
Nora Kocsis	Member until July 20, 2011
Finazzi Luca Santo	Member

INTESA SANPAOLO BANKA, D.D. BIH
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011
(all amounts are expressed in thousands of KM)

1. GENERAL (continued)

Management Board

Almir Krkalić	Director
Dario Grassani	Executive Director of Finance
Igor Bilandžija	Executive Director of Risk Management

Audit Committee

Giovanni Bergamini	Chairman
Alberto Gandini	Member
Andrea Perucchi	Member
Nicoletta Fusetti	Member
Damiano Accattoli	Member

Internal Auditor

Muamera Zuko

The shareholding structure is as follows:

	31 December 2011			31 December 2010		
	No. of shares	Amount KM '000	%	No. of shares	Amount KM '000	%
Shareholders						
IntesaSanpaolo Holding International S.A.	425,053	42,505	94.92	391,661	39,166	87.46
European Bank for Reconstruction and Development	-	-	-	32,478	3,248	7.25
Other	22,767	2,277	5.08	23,681	2,368	5.29
Total	447,820	44,782	100.00	447,820	44,782	100.00

INTESA SANPAOLO BANKA, D.D. BIH
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011
(all amounts are expressed in thousands of KM)

1. GENERAL (continued)

Nominal value of one share is KM 100.

In May 2011 EBRD sold shares to the majority shareholder IntesaSanpaolo Holding International S.A., Luxembourg, based on agreement on acquisition of equity. The sale was realized by EBRD through the Extraordinary Auction at the Sarajevo Stock Exchange.

The Bank has 60 priority (preference) shares with priority right in receipt of dividends. Also the Bank doesnot have any shares held by the entity or by its subsidiaries and no share reserved for issue under options and contracts for sale.

In the position of Reserves and retained earnings the Bank includes:

- Reserves for undistributed profit from previous years;
- Fair value reserves deriving from the revaluation of the AFS investments;
- Reserve for tax-deductible profit, in the measure of 15% of Bank's profit according to the then valid Income Tax Law (until 2002 year);
- Reserve for tax-deductible profit, in the measure of 75% of Bank's profit reinvested into fixed assets (until 2000 year);
- Reserve for undistributed dividends, following Supervisory Board decisions (until 1999 year);
- Revaluation reserve for fixed assets, according to valid Law (until 2001 year);
- Reserve for treasury shares.
- Reserve in capital formed upon applying new regulation with respect to the assessment of provisions for impairment of financial assets and contingent liabilities.

INTESA SANPAOLO BANKA, D.D. BIH
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011
(all amounts are expressed in thousands of KM)

2. ADOPTION OF NEW STANDARDS AND REVISED STANDARDS

2.1 Standards and Interpretations effective in the current period

Amendments resulting from Improvements to IFRSs to the following standards did not have any impact on the accounting policies, financial position or performance of the Bank:

- IFRIC 14 Prepayments of a Minimum Funding Requirement (Amended)
- IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments
- IAS 24 Related Party Disclosures (Amended)
- IAS 32 Classification on Rights Issues (Amended)
- IFRS 1 Limited Exemption from Comparative IFRS 7 Disclosures for the first time adopters (Amended)

Improvements to IFRSs

Other amendments resulting from Improvements to IFRSs to the following standards and interpretations did not have any impact on the accounting policies, financial position or performance of the Group:

- IFRS 1 First-time adoption
- IFRS 3 Business Combinations
- IFRS 7 Financial Instruments – Disclosures
- IAS 1 Presentation of Financial Statements
- IAS 27 Consolidated and Separate Financial Statements
- IAS 34 Interim Financial Reporting
- IFRIC 13 Customer Loyalty Programmers

2.2 Standards and Interpretations in issue not yet adopted

Standards issued but not yet effective up to the date of issuance of the Bank's financial statements are listed

below. This listing is of standards and interpretations issued, which the Bank reasonably expects to be applicable at a future date. The Bank intends to adopt those standards when they become effective. The Bank is in the process of assessing the impact of this amendment on the financial position or performance of the Bank.

- **IAS 1 Financial Statement Presentation (Amended) – Presentation of Items of Other Comprehensive Income**

The amendment is effective for annual periods beginning on or after 1 July 2012. The amendments to IAS 1 change the grouping of items presented in OCI. Items that could be reclassified (or 'recycled') to profit or loss at a future point in time would be presented separately from items that will never be reclassified. The amendment affects presentation only and has no impact on the Bank's financial position or performance.

- **IAS 12 Income Taxes (Amended) – Recovery of Underlying Assets**

The amendment is effective for annual periods beginning on or after 1 January 2012. The amendment clarified the determination of deferred tax on investment property measured at fair value. The amendment introduces a rebuttable presumption that deferred tax on investment property measured using the fair value model in IAS 40 should be determined on the basis that its carrying amount will be recovered through sale. Furthermore, it introduces the requirement that deferred tax on non-depreciable assets that are measured using the revaluation model in IAS 16 always be measured on a sale basis of the asset.

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2. ADOPTION OF NEW STANDARDS AND REVISED STANDARDS (continued)

2.2 Standards and Interpretations in issue not yet adopted (continued)

- **IAS 19 Employee Benefits (Amended)**

The amendment is effective for annual periods beginning on or after 1 January 2013. The IASB has issued numerous amendments to IAS 19. These range from fundamental changes such as removing the corridor mechanism and the concept of expected returns on plan assets to simple clarifications and re-wording. Early application is permitted.

- **IAS 27 Separate Financial Statements (Revised)**

The Standard is effective for annual periods beginning on or after 1 January 2013. As a consequence of the new IFRS 10 and IFRS 12, what remains of IAS 27 is limited to accounting for subsidiaries, jointly controlled entities, and associates in separate financial statements. Earlier application is permitted.

- **IAS 28 Investments in Associates and Joint Ventures (Revised)**

The Standard is effective for annual periods beginning on or after 1 January 2013. As a consequence of the new IFRS 11 and IFRS 12, IAS 28 has been renamed IAS 28 Investments in Associates and Joint Ventures, and describes the application of the equity method to investments in joint ventures in addition to associates. Earlier application is permitted.

- **IAS 32 Financial Instruments: Presentation (Amended) - Offsetting Financial Assets and Financial Liabilities**

The amendment is effective for annual periods beginning on or after 1 January 2014. This amendment clarifies the meaning of "currently has a legally enforceable right to set-off" and also clarifies the application of the IAS 32 offsetting criteria to settlement systems (such as central clearing house systems) which apply gross settlement mechanisms that are not simultaneous. The amendments to IAS 32 are to be retrospectively applied. Earlier application is permitted. However, if an entity chooses to early adopt, it must disclose that fact and also make the disclosures required by the IFRS 7 Offsetting Financial Assets and Financial Liabilities amendments.

- **IFRS 7 Financial Instruments: Disclosures (Amended) - Enhanced Derecognition Disclosure Requirements**

The amendment is effective for annual periods beginning on or after 1 July 2011. The amendment requires additional disclosure about financial assets that have been transferred but not derecognised to enable the user of the financial statements to understand the relationship with those assets that have not been derecognised and their associated liabilities. In addition, the amendment requires disclosures about continuing involvement in derecognised assets to enable the user to evaluate the nature of, and risks associated with, the entity's continuing involvement in those derecognised assets. The amendment has only disclosure effects.

- **IFRS 7 Financial Instruments: Disclosures (Amended) - Offsetting Financial Assets and Financial Liabilities**

The amendment is effective for annual periods beginning on or after 1 January 2013. The amendment introduces common disclosure requirements. These disclosures would provide users with information that is useful in evaluating the effect or potential effect of netting arrangements on an entity's financial position. The amendments to IFRS 7 are to be retrospectively applied.

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2. ADOPTION OF NEW STANDARDS AND REVISED STANDARDS (continued)

2.2 Standards and Interpretations in issue not yet adopted (continued)

- **IFRS 9 Financial Instruments - Classification and Measurement**

The new standard is effective for annual periods beginning on or after 1 January 2015. IFRS 9 as issued reflects the first phase of the IASBs work on the replacement of IAS 39 and applies to classification and measurement of financial assets and financial liabilities as defined in IAS 39. Phase 1 of IFRS 9 will have a significant impact on (i) the classification and measurement of financial assets and (ii) a change in reporting for those entities that have designated financial liabilities using the FVO. In subsequent phases, the IASB will address hedge accounting and impairment of financial assets. The completion of this project is expected over the first half of 2012. Early application is permitted.

- **IFRS 10 Consolidated Financial Statements**

The new standard is effective for annual periods beginning on or after 1 January 2013. IFRS 10 replaces the portion of IAS 27 Consolidated and Separate Financial Statements that addresses the accounting for consolidated financial statements. It also includes the issues raised in SIC-12 Consolidation — Special Purpose Entities. IFRS 10 establishes a single control model that applies to all entities including special purpose entities. The changes introduced by IFRS 10 will require management to exercise significant judgment to determine which entities are controlled, and therefore, are required to be consolidated by a parent, compared with the requirements that were in IAS 27.

- **IFRS 11 Joint Arrangements**

The new standard is effective for annual periods beginning on or after 1 January 2013. IFRS 11 replaces IAS 31 Interests in Joint Ventures and SIC-13 Jointly-controlled Entities — Non-monetary Contributions by Venturers. IFRS 11 removes the option to account for jointly controlled entities (JCEs) using proportionate consolidation. Instead, JCEs that meet the definition of a joint venture must be accounted for using the equity method.

- **IFRS 12 Disclosures of Involvement with Other Entities**

The new standard is effective for annual periods beginning on or after 1 January 2013. IFRS 12 includes all of the disclosures that were previously in IAS 27 related to consolidated financial statements, as well as all of the disclosures that were previously included in IAS 31 and IAS 28. These disclosures relate to an entity's interests in subsidiaries, joint arrangements, associates and structured entities. A number of new disclosures are also required.

- **IFRS 13 Fair Value Measurement**

The new standard is effective for annual periods beginning on or after 1 January 2013. IFRS 13 establishes a single source of guidance under IFRS for all fair value measurements. IFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under IFRS when fair value is required or permitted. This standard should be applied prospectively and early adoption is permitted.

- **IFRIC Interpretation 20 Stripping Costs in the Production Phase of a Surface Mine**

The interpretation is effective for annual periods beginning on or after 1 January 2013. This interpretation only applies to stripping costs incurred in surface mining activity during the production phase of the mine ('production stripping costs'). Costs incurred in undertaking stripping activities are considered to create two possible benefits a) the production of inventory in the current period and/or b) improved access to ore to be mined in a future period (stripping activity asset). Where cost cannot be specifically allocated between the inventory produced during the period and the stripping activity asset, IFRIC 20 requires an entity to use an allocation basis that is based on a relevant production measure. Early application is permitted.

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3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

3.1. Basis of presentation

These financial statements are prepared in accordance with accounting regulations applicable to financial reporting of banks in the Federation of Bosnia and Herzegovina.

As required by local legislation, the Bank prepares financial statements in accordance with International Financial Reporting Standards (IFRS) as published by the International Accounting Standards Board and as modified by the regulatory requirements prescribed by the Banking Agency of Federation of Bosnia and Herzegovina (FBA).

During 2011, the Bank applied new accounting policies in accordance with the Decision of minimum standards of credit risk management and classification of assets dated from January 2011 with respect of assessment of impairment of financial assets and contingent liabilities. Previously the Bank used the guidance of Federal Banking Agency described in Note 3.3. Based on new regulation the banks are required to apply IAS 39 and 37 for the assessment of impaired of financial assets and provisions for contingent liabilities as described in Note 3.3. – Impairment of financial assets and provisions for contingent liabilities.

The Bank restated opening balances of the Balance Sheet items and equity components as of December 2010 for the effect of applying new accounting policies. The difference arising between the previous balance of provisions and new assessed amount was credited to the special reserve within equity.

Since it was not practicable to restate the balance of earliest period of Financial Statement 31 December 2009, and as permitted by FBA, the Income Statement for the year 2010, presented as comparison information, was not restated, and accordingly it is not totally comparable with 31 December 2011 in the position of Impairment losses and provisions and Recoveries of written off loans.

The financial statements have been prepared on the historical cost basis except for certain non-current assets and financial instruments which are reported at fair value. The principal accounting policies are set out below.

The financial statements are presented in thousands of convertible mark (KM'000) which is the functional currency of the Bank.

The financial statements are prepared on an accrual basis of accounting, under the going concern assumption.

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and their reported amounts of revenues and expenses during the reporting period. These estimates are based on the information available as at the balance sheet date and actual results could differ from those estimates.

The Bank maintains its books of accounts and prepares financial statements for regulatory purposes in accordance with the regulations of the Banking Agency of Federation of Bosnia and Herzegovina (FBA) and Law on Banks of the Federation of Bosnia and Herzegovina.

INTESA SANPAOLO BANKA, D.D. BIH
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011
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3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3.2. Restatement of opening balances

As disclosed in Note 3.1. the Bank restated opening balances of the Balance Sheet items and equity components as of December 2010 for the effect of applying new accounting policies. The difference arising between the previous balance of provisions and new assessed amount was credited to the special reserve within equity.

The Bank restated opening balance as of 31 December 2010 with respect of adoption of new regulation in respect with assessment of impairment of financial assets and provisions for contingent liabilities.

The adjustment comprised of:

- Recognition on Balance Sheet previously fully written off assets classified in category "E" and 100% provisioned in accordance with previous Federal Banking Agency regulation and
- recording differences in provisions arising upon application of new regulation

The summary of the adjustments are presented below:

Note	Assets	Gross Assets	Provisions	Net Assets	Recognition of assets / provisions previously written off	Reversal of provisions	Gross Assets	Provisions	Net Assets
		Previously reported			Adjustments		Restated		
20	Loans and receivables	934,077	(43,217)	890,860	42,456	(16,938)	976,533	(68,735)	907,798
21	Assets available for sale	999	(20)	979	857	-	1,856	(877)	979
22	Other assets	9,730	(492)	9,238	2,970	-	12,700	(3,462)	9,238
29	Provisions for contingent liabilities	-	(2,637)	-	-	(1,341)	-	(1,296)	-
	Reserve in Capital – Total adjustment	-	-	-	-	18,279	-	-	-

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3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3.2. Restatement of opening balances (continued)

Income Statement Reclassifications

Certain amounts in the previous year financial statements have been reclassified to conform to the current year presentation:

The Bank reclassified income from service fees related to Frameworks Agreements for loans from Interest income position to Fee and Commission Income position. For consistency reasons, a similar item of 103 thousand KM has been reclassified in the 2010 Statement of Income.

The Bank reclassified expenses related to receiveguarantees from Interest Expense position to Fee and Commission Expenses. For consistency reasons, a similar item of 548 thousand KM has been reclassified in the 2010 Statement of Income.

3.3. Summary of accounting policies

Recognition of income and expense

Revenues are recognized when they are collected or, in case of sale of goods or products, when it is probable that the economic benefits will be received and these benefits may be measured reliably, in the case of services, when these have been rendered. In particular:

- interest is recognized on accrual on the basis of the contractual interest rate or the effective interest rate in the case of application of amortized cost;
- dividends are posted in the income statement in the financial year when their distribution is approved;
- commission income / expense from services is recorded, on the basis of the existence of contractual agreements, in the period in which the services have been rendered;
- revenues from the sale of financial instruments, determined by the difference between transaction amount paid or received and the fair value of the instrument, are recognized in the income statement at the time of the transaction;
- profits and losses from securities trading are recognized in the income statement at the date of sale, on the basis of the difference between the consideration paid or collected and the carrying value of such instruments;

Loan origination fees, after approval and drawdown of loans, are deferred (together with related direct costs) and recognized as an adjustment to the effective yield of the loan over its life.

Employee benefits

On behalf of its employees, the Bank pays pension and health insurance on and from salaries, which are calculated on the gross salary paid, as well as taxes, which are calculated on the net salary paid. The Bank is paying the above contributions into the Pension and Health Fund of the entities, as per the set legal rates during the course of the year on the gross salary paid. In addition, meal allowances, transport allowances and vacation bonuses are paid in accordance with the local legislation. These expenses are recorded in the income statement in the period in which the salary expense is incurred.

INTESA SANPAOLO BANKA, D.D. BIH
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011
(all amounts are expressed in thousands of KM)

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES(continued)

3.3. Summary of accounting policies (continued)

Retirement severance payments

According to the local legislation and internal Rulebook on employment, the Bank makes retirement severance payments of minimum three average monthly salaries of the employee in question or three average salaries of the Federation of Bosnia and Herzegovina paid in the period of the last three months, depending on what is more favourable to the employee.

Provision for retirement benefits is calculated by independent actuary. The liability recognized in the balance sheet is the present value of the obligation, determined by discounting estimated future outflows using the projected unit credit method. Actuarial gains and losses are recognized in income statement in the period in which they arise.

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax expense is based on taxable income for the year. Taxable income differs from net income as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Bank's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax basis used in the computation of taxable profit, and is accounted for using the balance sheet liability method.

Deferred tax liabilities are generally recognized for all taxable temporary differences and deferred tax assets are recognized to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilized.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the asset to be recovered. Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset realized. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority and the Bank has the ability and intention to settle on a net basis.

The Bank is subject to various indirect taxes which are included in administrative expenses.

Cash and cash equivalents

For the purpose of reporting cash flows, cash and cash equivalents are defined as cash, balances with the Central Bank ("CBBH") and current accounts with other banks.

Cash and cash equivalents exclude the compulsory minimum reserve with the Central Bank as these funds are not available for the Bank's day to day operations. The compulsory minimum reserve with the CBBH is a required reserve to be held by all commercial banks licensed in Bosnia and Herzegovina.

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NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011
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3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3.3. Summary of accounting policies (continued)

Financial assets

Financial assets are recognized and derecognized on a trade date where the purchase or sale of an investment is under a contract whose terms require delivery of the instrument within the timeframe established by the market concerned, and are initially measured at fair value, net of transaction costs, except for those financial assets classified as at fair value through profit or loss, which are initially measured at fair value.

Financial assets are classified into the following specified categories: financial assets as 'at fair value through profit or loss' (FVTPL), 'held-to-maturity investments' (HTM), 'available-for-sale' (AFS) financial assets and 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Financial assets at FVTPL

Financial assets are classified as at FVTPL where the financial asset is either held for trading or it is designated as at FVTPL.

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

- it has been acquired principally for the purpose of selling in the near future; or
- it is a part of an identified portfolio of financial instruments that the Bank manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

A financial asset other than a financial asset held for trading may be designated as at FVTPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial asset forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Bank's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- It forms part of a contract containing one or more embedded derivatives, and IAS 39 permits the entire combined contract (asset or liability) to be designated as at FVTPL.

Financial assets at FVTPL are stated at fair value, with any resultant gain or loss recognised in profit or loss. The net gain or loss recognised in profit or loss incorporates any dividend or interest earned on the financial asset.

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3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3.3. Summary of accounting policies (continued)

Financial assets (continued)

Financial assets at FVTPL (continued)

The fair values of financial assets and financial liabilities are determined as follows:

- the fair value of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market prices (mid price), without any deduction for transaction costs (so called 'first level' of fair value);
- the fair value of other financial assets and financial liabilities (excluding derivative instruments) are determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions (so called 'second level' of fair value which uses only insignificant adjustments to the market inputs);
- the fair value of derivative instruments, are calculated using quoted prices. Where such prices are not available use is made of discounted cash flow analysis using the applicable yield curve for the duration of the instruments for non-optional derivatives, and option pricing models for optional derivatives (so called 'second level' of fair value'), and
- Certain financial instruments are recorded at fair value using valuation techniques in which current market transactions or observable market data are not available. Their fair value is determined from input not directly visible on the market or prices of similar assets or deduced from non-active markets that are subject to significant adjustments (so called "third level" of fair value)

Financial liabilities are classified into the following specified categories: financial liabilities 'at fair value through profit or loss' (FVTPL), or "other financial liabilities".

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset or, where appropriate, a shorter period.

AFS financial assets

Available-for-sale investments include equity and debt securities. Equity investments classified as available-for-sale are those which are neither classified as held-for-trading nor designated at fair value through profit or loss. Debt securities in this category are those which are intended to be held for an indefinite period of time and which may be sold in response to needs for liquidity or in response to changes in the market conditions. The bank has not designated any loans or receivables as available-for-sale. After initial measurement, available-for-sale financial investments are subsequently measured at fair value.

Unrealized gains and losses are recognized directly in equity (other comprehensive income) in the 'Fair value reserves'. When the investment is disposed of, the cumulative gain or loss previously recognized in equity is recognized in the income statement in 'Other operating income'. Where the bank holds more than one investment in the same security they are deemed to be disposed of on a first-in first-out basis.

Interest earned whilst holding available-for-sale financial investments is reported as interest income using the EIR.

Dividends earned whilst holding available-for-sale financial investments are recognized in the income statement as 'Other operating income' when the right of the payment has been established.

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3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3.3. Summary of accounting policies (continued)

Financial assets (continued)

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

Loan and receivables are measured at initial recognition at fair value, and are subsequently measured at amortised cost using the effective interest method, less any allowance for impairment. Third party expenses, such as legal fees, incurred in securing a loan are treated as part of the cost of the transaction as well as fees received from customers.

Impairment of financial assets and provisions for contingent liabilities and commitments

According to the Federal Banking Agency *Decision of minimum standards of credit risk management and classification of assets dated from 2003* the Bank classified loans, other receivables, as well as contingent liabilities and commitments into the following categories:

- A – Performing assets;
- B – Special mention;
- C – Substandard;
- D – Doubtful loan and
- E – Loss.

For loans, receivables and off-balance sheet exposures classified as performing, a general allowance/provision equal to 2% of the outstanding exposure used to be made.

For exposures classified into categories from B to D the following range of provision applied:

B – Special mention	from 5 to 15%
C – Substandard	from 15 to 40%
D – Doubtful	from 41 to 60%
E – Loss	100%

Assets regarded as non-collectable were classified into category "E" and were fully provisioned and recorded in off-balance sheet. Subsequent recoveries were credited to "Collected write offs" in Income Statement.

After applying new regulation, *Decision of minimum standards of credit risk management and classification of assets* December 2010 and December 2011 (revised text), the process for assessment of impairment of financial assets and provisions for contingent liabilities and commitments are in accordance requirements of IAS 39 and IAS 37.

In particular, The Bank assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

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3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3.3. Summary of accounting policies (continued)

Financial assets (continued)

Impairment of financial assets and provisions for contingent liabilities and commitments (continued)

For amounts due from banks and loans to customers carried at amortised cost, the Bank first assesses individually whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. 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 in a group of financial assets with similar credit risks characteristics and collectively assesses them for impairment. 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.

If there is an objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the assets' carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Bank. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to the income statement.

The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

In particular, the Bank determines the allowances appropriate for each individually significant loan on an individual basis. Items considered when determining allowance amounts include the sustainability of the counterparty's business plan, its ability to improve performance once a financial difficulty has arisen, the availability of other financial support and the realisable value of collateral, and the timing of the expected cash flows. The impairment losses are evaluated on monthly basis.

Allowances are assessed collectively for losses on loans to customers that are not individually significant and for individually significant loans where there is not yet objective evidence of individual impairment. Allowances are evaluated at each reporting date with each portfolio receiving a separate review.

Collective assessment takes account of impairment that is likely to be present in the portfolio even though there is no objective evidence of impairment in an individual assessment. Impairment losses are estimated by taking into consideration the following information: historical losses in the portfolio or in portfolios having comparable (even if less favourable) credit risk characteristics; current economic conditions; the appropriate delay between the time a loss is likely to have been incurred and the time it will be identified as requiring an individually assessed impairment allowance; expected receipts and recoveries once impaired. The impairment allowance is then reviewed by credit management to ensure alignment with the Bank's overall policy.

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3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3.3. Summary of accounting policies (continued)

Financial assets (continued)

Impairment of financial assets and provisions for contingent liabilities and commitments (continued)

According to the Decision of minimum standards of credit risk management and classification of assets, the Bank is required to classify loans, other receivables, contingent liabilities and commitments into the categories A, B, C, D and E based on guidance prescribed in the Decision as well as to apply specific percentages to calculate the reserve for credit losses. If the calculated amount of the reserve for credit losses is higher than the total amount of allowances for impairment of financial assets and provisions for contingent liabilities and commitments recognized in balance sheet, the Bank is required to deduct the amount of shortfall from the regulatory capital in the calculation in the capital adequacy and other applicable regulatory ratios.

Derecognition of financial assets

The Bank derecognises a financial asset only when the contractual rights to the cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Bank neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Bank recognises its retained interest in the asset and an associated liability for amounts it may have to pay.

Property and equipment

Property and equipment are stated at cost less accumulated depreciation and accumulated impairment losses, if any. Cost includes the purchase price and directly associated cost of bringing the asset to a working condition for its intended use. Maintenance and repairs, replacements and improvements of minor importance are expensed as incurred. Significant improvements and replacement of assets are capitalised. Gains or losses on the retirement or disposal of property and equipment are included in the statement of income in the period in which they occur.

Properties in the course of construction are carried at cost, less impairment loss, if any. Depreciation commences first following month after the assets are ready for their use. Depreciation is calculated on a straight-line basis over the estimated useful life of the applicable assets and based upon the application of the following annual percentages to historical costs:

	31 December 2011	31 December 2010
Buildings	1.30% - 3.00%	1.30%
Furniture and other equipment	10.00%-20.00%	10.00%-20.00%
Computers	20.00%	20.00%
Leasehold improvements	20.00%	20.00%
Software	20.00%	20.00%

Property and equipment is derecognised on disposal or when no future economic benefits are expected from its use. Any gain or loss on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is recognised in 'Other operating income' in the income statement in the year the asset is derecognised.

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3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3.3. Summary of accounting policies (continued)

Financial liabilities and equity instruments issued by the Bank

Classification as debt or equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

Equity instruments

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Bank are recorded at the proceeds received, net of direct issue costs.

Payables

Amounts due to banks and due to customers (including subordinated debt) represent financial liabilities and include various forms of interest-bearing and non-interest-bearing funding on the interbank market and with customers and funding.

Initial recognition of such financial liabilities occurs at the date of subscription of the contract, which normally coincides with the time of collection of the sums deposited. Initial recognition is based on the fair value of the liabilities, normally equal to the amount collected, increased by any additional charges/revenues directly attributable to the single funding. Internal administrative costs are excluded.

After initial recognition, financial liabilities are measured at amortized cost using the effective interest rate method. An exception is made for short-term liabilities, which are stated at the payable amount as the time value is immaterial.

Financial liabilities are derecognised from the statement of financial position when they have expired or extinguished. The difference between book value of the liability and amount paid for repurchase is recorded in the income statement.

Other Provisions and Provisions for contingent liabilities

Provisions are recognized when the Bank has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the obligation can be made.

Other provisions record provisions relating to legal obligations, labor relationships or to litigation, also fiscal.

They are recognized in an amount that represents the best possible estimate of the expenditure required to settle the obligation that exists at the end of the reporting period. The best estimate required to settle the obligation is the amount that an entity would rationally pay at the end of the reporting period.

Provisions are measured according to the rule set forth in IAS 37 concerning the one-to-one correlation of the event and the associated provision and require management on a case-by-case basis.

Provisions made on an individual and collective basis, relative to estimated possible disbursements connected to credit risk relative to guarantees and commitments are recorded under the caption "provisions for contingent liabilities and commitments"

Derecognition of financial liabilities

The Bank derecognizes financial liabilities when, and only when, the Bank's obligations are discharged, cancelled or they expire.

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3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3.3. Summary of accounting policies (continued)

Off-balance sheet commitments

In the ordinary course of business, the Bank enters into credit related commitments which are recorded in off-balance sheet accounts and primarily include guarantees, letters of credit and undrawn loan commitments. Financial guarantee contract liabilities are measured initially at their fair values and are subsequently measured at the higher of:

- the amount of the provision assessed in accordance with IAS 37 and
- the amount initially recognised less, where appropriate, cumulative amortisation recognised in accordance with IAS 18 *Revenue*.

Foreign currency translation

Transactions in currencies other than Bosnia and Herzegovina KM are initially recorded at the rates of exchange prevailing on the dates of the transactions. Monetary assets and liabilities are translated at the rates prevailing on the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated. Profits and losses arising on translation are included in the statement of income for the period.

The Bank values its assets and liabilities by middle rate of Central Bank of Bosnia and Herzegovina valid at the date of balance sheet. The principal rates of exchange set forth by the Central Bank and used in the preparation of the Bank's balance sheet at the reporting dates were as follows:

31 December 2011	EUR 1= KM 1.95583	USD 1 = KM 1,511577
31 December 2010	EUR 1= KM 1.95583	USD 1 = KM 1,472764

Segment reporting

Management has monitored the operating results of the Bank as a single segment for the purpose of making decisions about resource allocations and performance assessment.

Regulatory requirements

The Bank is subject to the regulatory requirements of the Banking Agency of Federation of Bosnia and Herzegovina. These regulations include limits and other restrictions pertaining to minimum capital adequacy requirements, classification of loans and off balance sheet commitments and forming allowances to cover credit risk, liquidity, interest rate and foreign currency position. At year end the Bank was in compliance with all regulatory requirements.

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4. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the application of the Bank's accounting policies, which are described in note 3, the directors are required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Key sources of estimation uncertainty

The following are the key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

Useful lives of property, plant and equipment

As described above, the Bank reviews the estimated useful lives of property, plant and equipment at the end of each annual reporting period.

Impairment losses on loans and other placements

The Bank assesses at each statement of financial position date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred "loss event") and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated.

Evidence of impairment may include indicators that the borrower or a group of borrowers is experiencing significant financial difficulty, the probability that they will enter bankruptcy or other financial reorganization, default or delinquency in interest or principal payments and were observable data indicates that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Detail explanation of assessed process is described in Note 3.3. - *Impairment of financial assets and provisions for contingent liabilities and commitments.*

Long-term employee benefits

The cost of the long-term employee benefits is determined using actuarial valuation. The actuarial valuation involves making assumptions about discount rates, future salary increases, and future turnover rates. Due to the long term nature of these plans, such estimates are subject to significant uncertainty.

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4. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY
(continued)

Fair value of financial assets and liabilities

The directors use their judgment in selecting an appropriate valuation technique for financial instruments not quoted in an active market. Valuation techniques commonly used by market practitioners are applied. Financial instruments are valued using a discounted cash flow analysis based on assumptions supported, where possible, by observable market prices or rates. The estimation of fair value of unlisted shares includes some assumptions not supported by observable market prices or rates.

It is the opinion of the management of the Bank that the fair value of the Bank's financial assets and liabilities are not materially different from the amounts stated in the balance sheets as at 31 December 2011 and 31 December 2010. In estimating the fair value of the Bank's financial instruments, the following methods and assumptions are used:

Cash balances with the Central bank

The carrying values of cash and balances with the Central bank are generally deemed to approximate their fair value.

Due from banks

The estimated fair value of amounts due from banks that mature in 180 days or less approximates their carrying amounts. The fair value of other amounts due from banks is estimated based upon discounted cash flow analyses using interest rates currently offered for investments with similar terms (market rates adjusted to reflect credit risk).

Loans and advances to customers

The fair value of variable yield loans that regularly reprice, with no significant change in credit risk, generally approximates their carrying value. The fair value of loans at fixed interest rates is estimated using discounted cash flow analyses, based upon interest rates currently offered for loans with similar terms to borrowers of similar credit quality.

Amounts due to banks and customers

The fair value of term deposits payable on demand represents the carrying value of amounts payable on demand as at the balance sheet date. The fair value of term deposits at variable interest rates approximates their carrying values as at the balance sheet date. The fair value of deposits at fixed interest rates is estimated by discounting their future cash flows using rates currently offered for deposits of similar remaining maturities.

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5. INTEREST INCOME

	2011	2010
Companies	37,177	31,642
Individuals	38,772	38,291
Banks and other financial institutions	2,018	1,517
Interest for AFS	122	42
Other	225	150
	78,314	71,642

6. INTEREST EXPENSE

	2011	2010
Companies	9,152	9,496
Individuals	7,375	7,884
Banks and other financial institutions	7,115	4,232
Other	230	303
	23,872	22,015

7. FEE AND COMMISSION INCOME

	2011	2010
Domestic payment transactions	3,101	2,857
Credit card activities	3,143	2,734
Foreign payment transactions	2,413	2,106
FX transactions	1,720	1,019
Guarantees and letter of credits	1,563	1,296
Agency services	108	126
Other	2,348	2,258
	14,396	12,396

8. FEE AND COMMISSION EXPENSE

	2011	2010
Credit card operations	2,068	1,948
Central Bank BiH	221	208
Commission on received guarantees and other services	643	548
Domestic payment transactions	513	450
E-banking service	125	121
	3,570	3,275

9. NET FOREIGN EXCHANGE INCOME

	2011	2010
Gains on foreign exchange transactions and translations	27,838	30,356
Loss on foreign exchange transactions and translations	(26,529)	(28,889)
	1,309	1,467

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10. OTHER OPERATING INCOME

	<u>2011</u>	<u>2010</u>
Rental income	6	-
Dividend income	35	-
Gain on sale of AFS investments	7	87
Gain on sale of property	20	62
Recoveries of claims from legal proceedings	-	391
Other income	368	369
	<u>436</u>	<u>909</u>

11. PERSONNEL EXPENSES

	<u>2011</u>	<u>2010</u>
Wages and salaries	13,236	12,547
Social security costs	5,839	5,512
Provisions, net, for retirement and other employee benefits (Note 28)	41	35
Other expenses	172	166
	<u>19,288</u>	<u>18,260</u>

The Bank does not have pension arrangements separate from Bosnia and Herzegovina pension system. This system requires that current contributions by the employer should be calculated as a percentage of current gross salary payments and taxes on net salary; these expenses are charged to the profit and loss statement in the period the related compensation is earned by the employee.

The average number of personnel employed by the Bank during the years ended 31 December 2011 and 31 December 2010 was 521 and 515 respectively.

12. ADMINISTRATIVE EXPENSES

	<u>2011</u>	<u>2010</u>
Rent and other rent related expense	3,342	3,314
Telecommunication and post expense	2,701	2,541
Saving deposit insurance and other insurance charges	1,594	1,472
Provisions, net, for legal proceedings (Note 28)	318	258
Material expenses	1,150	1,125
Representation and marketing expense	936	942
Consultancy and the Banking Agency of FBiH expenses	1,203	1,318
Energy	874	771
Maintenance expenses	2,720	2,508
Security and transport costs	2,055	1,868
Other expenses	1,077	1,136
	<u>17,970</u>	<u>17,253</u>

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13. IMPAIRMENT LOSSES AND PROVISIONS

	<u>2011</u>	<u>2010</u>
Additions on impairment losses on placements with other banks, net (Note 19)	(18)	3
Additions on impairment losses on loans and advances originated by the Bank, net (Note 20)	12,382	17,717
Additions (Release) of impairment losses on assets available for sale, net (Note 21)	(7)	9
Additions on provision for other assets, net (Note 22)	17	148
Additions on provision for commitments and contingent liabilities, net (Note 30)	1,045	631
	<u>13,419</u>	<u>18,508</u>

14. RECOVERIES OF WRITTEN OFF LOANS

	<u>2011</u>	<u>2010</u>
Suspended Interest	-	490
Principal	-	4,139
Other	-	114
	<u>-</u>	<u>4,743</u>

According the new Federal Banking Agency regulation, as described in Note 3.3 Impairment of financial assets and provision for contingent liabilities, income from recoveries of fully provisioned assets in 2011 is reported as part of position 13, Impairment losses and provisions.

As described in Note 3.2. in accordance with previous regulation of FBA the Bank fully written off loans in Ecategory reordered in Off Balance Sheet. Collection of those receivables was reported as "Recoveries of written off loans" in Income Statement.

15. INCOME TAX

	<u>2011</u>	<u>2010</u>
Profit before income tax	11,515	6,944
Non-deductible expenses and taxable income relieves	555	1,891
Taxable income	12,070	8,835
Income tax liability at the rate of 10%	<u>1,207</u>	<u>883</u>

Tax liability is based on accounting income before restatement taking into the account non-deductible expenses and non-taxable income. Tax income rate for the years ended 31 December 2011 and 31 December 2010 was 10%.

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16. EARNINGS PER SHARE

	31 December 2011	31 December 2010
Net profit	10,308	6,061
Weighted average number of ordinary shares outstanding	447,760	449,886
Basic earnings per share	0.02303	0.01347

The Bank does not have dilutive potential ordinary shares.

17. CASH AND CASH EQUIVALENTS

	31 December 2011	31 December 2010
Current account in domestic currency with the Central Bank	132,200	40,998
Cash on hand in domestic currency	14,854	14,040
Cash on hand in foreign currency	9,895	7,569
Correspondent accounts with banks in foreign currency	6,842	3,757
	163,791	66,364

18. OBLIGATORY RESERVE WITH THE CENTRAL BANK

	31 December 2011	31 December 2010
Obligatory reserve	71,158	97,789
	71,158	97,789

Minimum obligatory reserve as of 31 December 2011 is calculated in amount of 14% for deposits and borrowings with maturity up to one year and 7% for deposits and borrowings with maturity over one year for each working day during 10 calendar days following the period of maintaining the obligatory reserve. Mandatory reserve doesnot include local inter-bank deposits, short term and long term deposits from non-residents and short term and long term loans from non-residents, with effect from 1 November 2008.

19. PLACEMENTS WITH OTHER BANKS

	31 December 2011	31 December 2010
Short-term placements with banks from OECD countries	31,528	190,290
Less: Provisions for impairment	(8)	(26)
	31,520	190,264

The average interest rate for placements in EUR was 0.86% p.a. and 0.51% p.a. and for placements in USD 0.25% p.a. and 0.24% p.a. as of 31 December 2011 and 31 December 2010, respectively.

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19. PLACEMENTS WITH OTHER BANKS (continued)

The movements in the provision for impairment of placements with other banks are as follows:

	31 December 2011	31 December 2010
Balance as at 1 January	26	23
Provisions, net change (Note 13)	(18)	3
Balance as at 31 December	8	26

20. LOANS AND RECEIVABLES

	31 December 2011	31 December 2010 restated
Short-term loans in domestic currency	339,856	313,419
Short-term loans in foreign currency	3,204	2,935
Current portion of long-term loans	170,810	137,648
Total short-term loans	513,870	454,002
Long-term loans in domestic currency	748,717	647,810
Long-term loans in foreign currency	5,273	12,369
(Current portion of long-term loans)	(170,810)	(137,648)
Total long-term loans	583,180	522,531
<i>Total loans before provisions</i>	<i>1,097,050</i>	<i>976,533</i>
Provision for impairment	(78,441)	(68,735)
	1,018,609	907,798

Restatements of opening balances are disclosed in Note 3.2.

As of 31 December 2011, short-term and long-term loans in domestic currency include loans disbursed and repayable in domestic currency index-linked to the KM:EUR exchange rate in the amount of KM26,506thousand and KM742,412thousand, respectively (2010: KM16,331thousand and KM628,348thousand, respectively).

Short-term loans are granted for periods of up to 365 days. The majority of short-term loans in domestic currency are granted to clients for working capital financing. Long-term loans are mostly granted to individuals for housing and vehicle purchases, and to corporate clients for investment purposes.

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20. LOANS AND RECEIVABLES (continued)

The movements in the provision for impairment of loans are summarized as follows:

	31 December 2011	31 December 2010
Balance as at 1 January before restatement	43,217	39,289
Provisions for loans in off balance sheet (Note 3.2.)	42,456	-
Release of provisions based on IAS 39 (Note 3.2.)	(16,938)	-
Balance as at 1 January after restatement	68,735	-
Provisions charged (Note 13)	12,382	17,717
Reversal of provisions credited to deferred income	-	(236)
Permanent write off loans and receivables (Note 33)	(2,676)	-
Write-offs (Note 33)	-	(13,553)
Balance as at 31 December	78,441	43,217

	31 December 2011	31 December 2010 restated
Manufacturing industry	172,474	160,718
Trade	272,579	209,680
Construction industry	48,660	43,490
Services, finance, sport, tourism	23,933	21,862
Administrative and other public institutions	22,022	22,067
Agriculture, forestry, mining and energy	32,862	24,096
Transport and telecommunications	37,257	41,756
Other	37,620	36,525
Citizens	449,643	416,339
Loans and receivables, gross	1,097,050	976,533

	31 December 2011	31 December 2010 restated
Corporate Lending	647,407	560,194
Consumer Lending	254,088	235,196
Residential Mortgages	141,569	130,064
Credit and Debit Cards	53,986	51,079
Loans and receivables, gross	1,097,050	976,533

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20. LOANS AND RECEIVABLES (continued)

Interest rates for granted loans as at 31 December 2011 and 2010 are summarized as follows:

	31 December 2011		31 December 2010	
	KM '000	Annual interest rate	KM '000	Annual interest rate
<i>Domestic currency</i>				
Companies	639,449	3.32% - 10.86%	546,194	2.70% - 12.00%
Citizens	449,124	2.00% - 12.97%	415,303	2.00% - 12.75%
<i>Foreign currency</i>				
Companies	7,958	4.00% - 13.00%	14,000	3.76% - 7.02%
Citizens	519	5.50% - 10.99%	1,036	5.00% - 10.00%
	1,097,050		976,533	

21. ASSETS AVAILABLE FOR SALE

	31 December 2011	31 December 2010 restated
Debt instruments – the Government of Federation of Bosnia and Herzegovina bonds and treasury bills	15,333	440
Equity instruments	660	1,416
Total gross value	15,993	1,856
Impairment	(60)	(877)
	15,933	979

Restatements of opening balances are disclosed in Note 3.2.

Assets available for sale include investments of 20.03% in share capital of Bamcardd.d. Sarajevo in the amount of KM 488 thousand (2010: KM 488 thousand).

Also, assets available for sale include investments of less than 1% in various companies in Bosnia and Herzegovina recognized at cost of KM 172 thousand (2010: KM 928 thousand).

The movements in the provision for impairment of financial assets available for sale are summarized as follows:

	31 December 2011	31 December 2010
Balance as at 1 January before restatement	20	11
Provisions for AFS in off balance sheet (Note 3.2)	857	-
Balance as at 1 January after restatement	877	-
Permanent write off AFS (Note 33)	(810)	-
Provisions (Note 13)	(7)	9
Balance as at 31 December	60	20

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22. OTHER ASSETS

	31 December 2011	31 December 2010 restated
Prepaid income taxes	2,748	2841
Payment to the Cantonal Privatization Agency for Privatization of "Projekt" d.d. Sarajevo	1,200	1,200
Prepaid expenses	2,529	2,167
Fees receivable	626	442
Receivables from card operations	1,308	715
Assets acquired on foreclosed loans	646	1,975
Other assets	2,822	3,360
Total other assets	11,879	12,700
Provision for impairment	(2,839)	(3,462)
	9,040	9,238

Restatements of opening balances are disclosed in Note 3.2.

The movements in the provision for impairment of other assets are summarized as follows:

	31 December 2011	31 December 2010
Balance as at 1 January before restatement	492	590
Provisions for Other assets in off balance sheet (Note 33)	2,970	-
Balance as at 1 January after restatement	3,462	-
Permanent write off (Note 33)	(362)	
Provisions (Note 13)	17	148
Transfer to provisions for assets received in collection (Note 23)	(278)	-
Write-offs (Note 33)	-	(246)
Balance as at 31 December	2,839	492

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23. PROPERTY, PLANT AND EQUIPMENT

	Land and Buildings	Computers and other equipment	Software	Constru- ction in progress	Leasehold improve- ments	Total
<i>Cost value</i>						
31 December 2009	12,940	18,520	5,556	224	8,151	45,391
Additions	-	-	-	2,414	-	2,414
Disposals	(157)	(413)	-	(56)	-	(626)
Transfers from construction in progress	79	1,751	616	(2,522)	76	-
31 December 2010	12,862	19,858	6,172	60	8,227	47,179
Additions	-	-	-	3,455	-	3,455
Transfer from assets received in collections	1,267	-	-	-	-	1,267
Disposals	(3)	(758)	(1,095)	-	-	(1,856)
Transfers from construction in progress	73	2,122	998	(3,351)	158	-
31 December 2011	14,199	21,222	6,075	164	8,385	50,045
<i>Accumulated Depreciation</i>						
31 December 2009	1,249	9,011	2,931	-	3,840	17,031
Depreciation for the period	167	2,518	855	-	1,362	4,902
Disposals	(51)	(307)	-	-	-	(358)
31 December 2010	1,365	11,222	3,786	-	5,202	21,575
Depreciation for the Period	233	2,522	818	-	1,249	4,822
Disposals	-	(684)	(1,093)	-	-	(1,777)
31 December 2011	1,598	13,060	3,511	-	6,451	24,620
Net book value: 31 December 2010	11,497	8,636	2,386	60	3,025	25,604
Net book value: 31 December 2011	12,601	8,162	2,564	164	1,934	25,425

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24. DUE TO BANKS AND OTHER INSTITUTIONS

	31 December 2011	31 December 2010
Current portion of long-term borrowings	136,798	53,771
Total short-term borrowings	136,798	53,771
Long-term borrowings from foreign banks and other institutions	330,114	304,258
Long-term borrowings from domestic banks and other institutions	3,987	7,162
Current portion of long-term borrowings	(136,798)	(53,771)
Total long-term borrowings	197,303	257,649
Current accounts in domestic currency	3	3
Current accounts in foreign currency	-	4
Total current accounts	3	7
Short-term deposit	107,573	136,928
Long-term deposits	265	942
	441,942	449,297

Long-term borrowings from international banks and other institutions as at 31 December 2011 and 31 December 2010 are as follows:

	31 December 2011	31 December 2010
European Investment Bank	140,287	93,645
Commerzbank Ag Frankfurt, Germany	68,467	68,465
European Fund for Southeast Europe (EFSE), Luxembourg	42,833	44,787
Société Européenne De Banque S.A., Luxembourg	-	29,500
European Bank for Reconstruction and Development, London, UK	39,494	25,436
Vseobecna Uverova Banka A.S. Bratislava	19,660	19,640
Intesa Sanpaolo SPA Milan, Italy	15,425	18,595
KfWKreditanstalt für Wiederaufbau	3,948	3,936
Federalno ministarstvo finansija, Sarajevo	2,430	2,446
Vlada SBH/ŽSB, Travnik	-	2,134
Federalni zavod za zapošljavanje, Sarajevo	438	1,229
Federalno ministarstvo šumarstva i vodoprivrede, Sarajevo	1,028	1,028
Razvojna banka Federacije Bosne i Hercegovine d.o.o. Sarajevo	65	295
OPEC FUND for International Development, Vienna, Austria	-	255
Služba za zapošljavanje SBK / ŽSB	26	29
	334,101	311,420

Interest rates for long-term borrowings from banks and other institutions were in the range from 0% to 4.59% per annum and from 0% to 4.13% per annum as of 31 December 2011 and 31 December 2010, respectively.

Interest rate for short term deposits was in the range from 1.09% to 3.72% per annum and from 1.14% to 3.72% per annum as of 31 December 2011 and 31 December 2010, respectively.

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25. SUBORDINATED DEBT

	31 December 2011	31 December 2010
Ministarstvo finansija i trezora BiH	1,083	1,244
	1,083	1,244

The subordinated loan from Ministry of Finance and Treasury as of 31 December 2010 and 31 December 2011, respectively amounting to KM 1,244 thousand and KM 1,083 thousand was received in August 2003 in the amount of KM 2,408 thousand, and it is repayable in 60 quarterly instalments starting from 1 December 2003 until 1 September 2018. Interest rate is fixed at 2.3163 % p.a.

According to the approval of the Banking Agency of Federation of Bosnia and Herzegovina, the subordinated debt may be used as additional capital for calculation of regulatory capital.

26. DUE TO CUSTOMERS

	31 December 2011	31 December 2010
Demand deposits:		
Citizens:		
In KM	59,370	51,785
In foreign currencies	33,884	33,206
<i>Subtotal</i>	93,254	84,991
Legal entities:		
In KM	243,454	246,007
In foreign currencies	40,194	39,044
<i>Subtotal</i>	283,648	285,051
Total demand deposits	376,902	370,042
Term deposits:		
Citizens:		
In KM	33,989	28,833
In foreign currencies	142,868	132,587
<i>Subtotal</i>	176,857	161,420
Legal entities:		
In KM	89,053	88,631
In foreign currencies	76,597	69,504
<i>Subtotal</i>	165,650	158,135
Total term deposits	342,507	319,555
	719,409	689,597

During 2011 interest rates for demand deposits were from 0.00% to 2.50% per annum (during 2010 were from 0.00% to 2.50% per annum).

Short-term deposit interest rates were from 0.00% to 5.56% and from 0.00% to 7.20% per annum, during 2011 and 2010 respectively. Long-term deposit interest rates were from 0.00% to 8.00% and from 0.00% to 8.00% per annum, during 2011 and 2010 respectively.

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26. DUE TO CUSTOMERS (continued)

As of 31 December 2011, 'Due to Customers' includes deposits held as collateral for loans, guarantee and L/C in the amount of KM 17.889 thousand (2010:KM15.729thousand).

	31 December 2011	31 December 2010
Large Corporate customers:	373,928	342,198
Current Accounts	226,670	232,438
Term Deposits	147,258	109,760
Small and medium-sized enterprises:	75,371	100,988
Current Accounts	56,060	52,613
Term Deposits	19,311	48,375
Retail Customers:	270,110	246,411
Current Accounts	93,254	84,991
Term Deposits	176,856	161,420
	719,409	689,597

27. OTHER LIABILITIES

	31 December 2011	31 December 2010
Loan repayments received before due dates	3,066	2,631
Liabilities to vendors	1,375	1,054
Liabilities for employees bonuses	1,629	1,100
Managed fund difference (Note 31)	146	182
Credit card liabilities	230	61
Liabilities to shareholders	140	141
Deferred tax liability	1	1
Other liabilities	3,665	1,656
	10,252	6,826

Deferred tax liability relates to taxable temporary differences arising on fair value adjustments of financial assets available for sale. The effect of the fair value adjustment, net of relating tax for KM 1 thousand (2010: KM 1 thousand), is recognized through equity.

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28. OTHER PROVISIONS

	31 December 2011	31 December 2010
Provisions for litigations with the Tax authorities and clients	2,156	1,838
Provisions for retirement employee benefits and other short-term employee benefits	483	461
	2,639	2,299

Provisions for litigations depend on the uncertainty in the outcomes of the ongoing court cases with the tax authority and other proceedings.

	Provisions for legal proceedings (Note 12)	Provisions for retirement employee benefits and other short term employee benefits (Note 11)	Total
Balance at 31 December 2010	1,838	461	2,299
Additional provision recognised	370	74	444
Release of provision	(52)	(33)	(85)
Reductions arising from payments	-	(19)	(19)
Balance at 31 December 2011	2,156	483	2,639

Calculation of provisions for retirement benefits of KM 222 thousand as of 31 December 2011 (2010: KM 215 thousand) is performed by an independent actuary, applying a discount rate of 6% and 3% expected rate of increase in salaries, to working life and average salary of each employee.

Provisions for unused days of vacation of KM 261 thousand as of 31 December 2011 (2010: KM 246 thousand) are calculated for every employee, taking as a basis his/her salary and unused days of vacation.

In the ordinary course of business, the Bank has been involved in a number of legal proceedings to recover collateral or outstanding credit balances, as well as related interest and expenses from defaulted credit customers and interbank counterparts. The management of the Bank believes that any legal proceedings pending as at 31 December 2011 will not result in material loss to the Bank.

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29. FINANCIAL COMMITMENTS AND CONTINGENCIES

In the ordinary course of business, the Bank enters into credit related commitments which are recorded in off-balance sheet accounts and primarily include guarantees, letters of credit and undrawn loan commitments.

	31 December 2011	31 December 2010
Contingent liabilities		
Payment guarantees	34,483	23,833
Performance guarantees	30,746	24,330
Letters of credit	572	6,195
Total contingent liabilities	65,801	54,358
Commitments		
Unused portion of overdraft loans	111,008	72,791
Total commitments	111,008	72,791
Total contingent liabilities and commitments	176,809	127,149

Provisions for contingent liabilities are recognised when the Bank has a present obligation as a result of a past event, and it is probable that the Bank will be required to settle that obligation. Management Board estimates the provisions based at the best estimate of expenditure to settle the Bank's obligation.

Restatements of opening balances of provisions are disclosed in Note 3.2.

Movements in provision for contingent liabilities and commitments are as follows:

	31 December 2011	31 December 2010
Balance as at 1 January before restatement	2,637	2,709
Release of provisions according IAS 37	(1,341)	-
Balance as at 1 January after restatement	1,296	-
Increase in provisions (Note 13)	1,045	631
Write offs (Note 33)	-	(703)
Balance as at 31 December	2,341	2,637

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30. RELATED-PARTY TRANSACTIONS

Related parties, as defined by IAS 24, are those counter parties that represent:

- a. enterprises that directly, or indirectly through one or more intermediaries, control, or are controlled by, or are under common control with, the reporting enterprise (this includes holding companies, subsidiaries and fellow subsidiaries);
- b. associates – enterprises in which the Bank has significant influence and which is neither a subsidiary nor a joint venture of the investor;
- c. individuals owning, directly or indirectly, an interest in the voting power of the Bank that gives them significant influence over the Bank, and anyone expected to influence, or be influenced by, that person in their dealings with the Bank;
- d. key management personnel, that is, those persons who have authority and responsibility for planning, directing and controlling the activities of the Bank, including directors and officers of the Bank and close members of the families of such individuals; and
- e. Enterprises in which a substantial interest in the voting power is owned, directly or indirectly, by any person described in (c) or (d) or over which such a person is able to exercise significant influence. This includes enterprises owned by directors or major shareholders of the Bank and enterprises that have a member of key management in common with the Bank.

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30. RELATED-PARTY TRANSACTIONS (continued)

In considering each possible related party relationship, attention is directed to the substance of the relationship, and not merely the legal form.

	31 December 2011	31 December 2010
Receivables		
Key management personnel and close family members	403	423
Bank accounts and loans –IntesaSanpaolo Group	5,391	37,264
Other receivables –IntesaSanpaolo Group	82	110
	5,876	37,797
Liabilities		
Deposits - Key management personnel and close family members	915	731
Borrowings and term deposits –IntesaSanpaolo Group	143,102	204,356
Other liabilities -IntesaSanpaolo Group	318	1,326
Borrowings and other liabilities to European Bank for Reconstruction and Development (EBRD)	-	25,436
	144,335	231,849
Financial commitments and contingencies		
Guarantees issued in favour of IntesaSanpaolo Group	-	1,883
Commitments to lend - Key management personnel and close family members	109	73
Commitments to lend –IntesaSanpaolo Group	400	-
	509	1,956
Income		
Interest income - Key management personnel and close family members	31	23
Interest income - Intesa Sanpaolo Group	638	412
Other Income - Intesa Sanpaolo Group	112	120
	781	555

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30. RELATED-PARTY TRANSACTIONS (continued)

Expenses	31 December 2011	31 December 2010
Interest expense - Key management personnel and close family members	16	6
Interest expense - Intesa Sanpaolo Group	3,031	3,340
Interest expense - European Bank for Reconstruction and Development (EBRD)	2,317	1,712
Other expenses - Intesa Sanpaolo Group	500	570
Other expense - European Bank for Reconstruction and Development (EBRD)	41	62
	5,905	5,690

Intesa Sanpaolo Holding International S.A. is the majority shareholder and exercises control over the Bank's operations.

In May 2011, EBRD sold shares to majority shareholder Intesa Sanpaolo Holding International S.A., Luxembourg, based on agreement on acquisition of equity. The sale was realized by EBRD through the Extraordinary Auction at the Sarajevo Stock Exchange, after which EBRD is no longer considered to be related party. However, transactions with EBRD affecting Income statement during 2011 by the date of selling the shares are included in Income and Expenses within Note 30.

No exposure towards related parties has been classified as non-performing.

The remuneration of directors and other members of key management are as follows:

	31 December 2011	31 December 2010
Compensation for directors and other key management	476	481
Taxes and contributions on compensation	453	495
Bonuses to the Management Board - accrued expenses	446	448
Compensations for Supervisory Board members	29	29
Other Management benefits	71	165
	1,475	1,618

The Bank has:

- neither guarantee with any director or other member of key management,
- nor exposure towards director or key management has been classified as non-performing.

During the period all exposure were classified as performing.

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31. MANAGED FUNDS

The Bank manages assets on behalf of third parties. These assets are recorded separately from the Bank's assets. For its services, the Bank charges a fee amounting from 0.0% to 2.5% p.a. (in 2010 from 0.0% to 2.50% p.a.) of the total amount contributed.

	31 December 2011	31 December 2010
Liabilities		
Government organizations	9,187	9,105
Associations and Agencies	2,512	4,492
Banks and Insurance companies	1,384	3,555
Other	458	920
Total	13,541	18,072
Assets		
Loans to companies	12,799	16,813
Loans to citizens	596	1,077
Total	13,395	17,890
Amounts due to original creditors – managed funds (Note 27)	146	182

The Bank has not issued any guarantees related to manage funds.

32. CAPITAL MANAGEMENT

The Bank's objectives when managing capital, which is a broader concept than the 'equity' on the face of balance sheets, are:

- To comply with the capital requirements set by the regulators of the banking markets;
- To safeguard the Bank's ability to continue as a going concern so that it can continue to provide returns for shareholders and benefits for other stakeholders; and
- To maintain a strong capital base to support the development of its business.

The Bank expects to maintain its debt to capital ratio. Solvency indicators are as follows:

	31 December 2011	31 December 2010 restated
Debt (i)	1,161,351	1,138,894
Cash on hand, balances with the Central bank and placements with other banks	(266,469)	(354,417)
Net debt	894,882	784,477
Capital (ii)	158,893	148,721
Net debt to capital ratio	5.63	5.27

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32. CAPITAL MANAGEMENT (continued)

Debt (i) is defined as liabilities to banks and clients presented in detail in Notes and Capital (ii) includes total capital, Bank's reserves, retained earnings and subordinated debt.

Capital adequacy and the use of regulatory capital are monitored daily by the Bank's management employing techniques based on the guidelines developed by the Banking Agency of Federation of Bosnia and Herzegovina (FBA) for supervisory purposes. The required information is filed with the FBA on a quarterly basis.

The FBA requires each bank to:

- (a) hold the minimum level of the regulatory capital of KM 15,000 thousand, and
- (b) maintain a ratio of total regulatory capital to the risk-weighted asset at or above the minimum of 12% for 2011. From 31 December 2008, Federal Banking Agency requested banks to include in the calculation of capital adequacy a charge for operational risk.

As of 31 December 2009, the Federal Banking Agency changed the methodology for the calculation of the charge for operational risk, which is based on gross income.

The Bank's regulatory capital is divided into two tiers:

- Tier 1 capital or Core Capital: share capital (net of any book values of the treasury shares), share premium, retained earnings and reserves created by appropriations of retained earnings; unrealised gains/losses arising on the fair valuation of equity instruments held as available for sale and
- Tier 2 capital or Supplementary Capital: qualifying principle of subordinated loan capital, collective impairment allowances and profit for the year.

According to the Decision of minimum standards of credit risk management and classification of assets, the Bank is required to classify loans, other receivables, contingent liabilities and commitments into the categories A, B, C, D and E based on guidance prescribed in the Decision as well as to apply specific percentages to calculate the reserve for credit losses. If the calculated amount of the reserve for credit losses is higher than the total amount of allowances for impairment of financial assets and provisions for contingent liabilities and commitments recognized in balance sheet, the Bank is required to deduct the amount of shortfall from the regulatory capital in the calculation in the capital adequacy and other applicable regulatory ratios.

The risk-weighted assets are measured by means of a hierarchy of four weights classified according to the nature of – and reflecting an estimate of credit, market and other risks associated with – each asset and counterparty, taking into account any eligible collateral or guarantees. A similar treatment is adopted for off-balance sheet exposure, with some adjustments to reflect the more contingent nature of the potential losses.

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32. CAPITAL MANAGEMENT (continued)

The table below summarises the composition of regulatory capital and the ratios of the Bank. The Bank complies with all of the externally imposed capital requirements.

	31 December 2011	31 December 2010
Tier 1 capital		
Share Capital	44,782	44,782
Treasury shares	-	-
Share Premium	57,415	57,415
Statutory reserves	614	614
Retained Earnings	20,858	14,797
Other reserves not related to assets valuation	5,535	5,536
Revaluation reserve – available for sale investments	19	(7)
Items to be deducted: Intangible assets	(2,631)	(2,395)
Total qualifying Tier 1 Capital	126,592	120,742
Tier 2 capital		
Qualifying subordinated loan capital	1,083	1,244
Generic provisions for performing assets	21,814	19,459
Profit for the year	10,308	6,061
Total qualifying Tier 2 Capital	33,205	26,764
Deductible item		
Negative difference between allowances for impairment and provisions for contingent liabilities and commitments and the regulatory reserves for credit losses	(7)	-
Total regulatory capital	159,790	147,506
Risk weighted assets		
On balance sheet	993,408	955,585
Off balance sheet	102,212	72,649
Total	1,095,620	1,028,234
Operational risk	71,955	61,559
Total weighted risk	1,167,575	1,089,793
Capital adequacy ratio	13,68%	13,53%

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33. FINANCIAL INSTRUMENTS

Financial risk management objectives

Main purpose of Risk Management Department is to support financial operations, coordinate access to domestic and international financial markets, overlook and manage financial risk through internal risk reports including analysis by size and level of the risk. Financial risk management includes: market risk (FX risk, interest rate risk, and pricing risk), credit risk, liquidity risk and interest rate cash flow risk.

FX Value-at-Risk is individual, concise, statistic measurement of possible losses in the portfolio. Value-at-Risk is loss measurement in normal movements of risk factors on the market. Losses higher than the Value-at-Risk occur only with a low indicated likelihood.

The main model assumptions are:

- Being based on the Historical methodology,
- 99 percent as a confidence interval for VaR computation,
- One-day held period.

The model covers foreign currency risk – valid for foreign currency transactions and positions denominated on foreign currencies; resulting from foreign currency rate volatility.

The model can compute VaR at different aggregation levels – from a single position to any sub-portfolio level. Therefore, the model allows a detailed analysis of risk profiles of multi-level portfolio hierarchy and diversity effects occurring. Furthermore, VaR measurement can be expounded based on risk source (risk factors). These features of a more detailed risk monitoring allow determining an efficient limit structure which can be compared through different organisational units.

Key data and their sources, necessary for daily VaR computation based on this model are as follows:

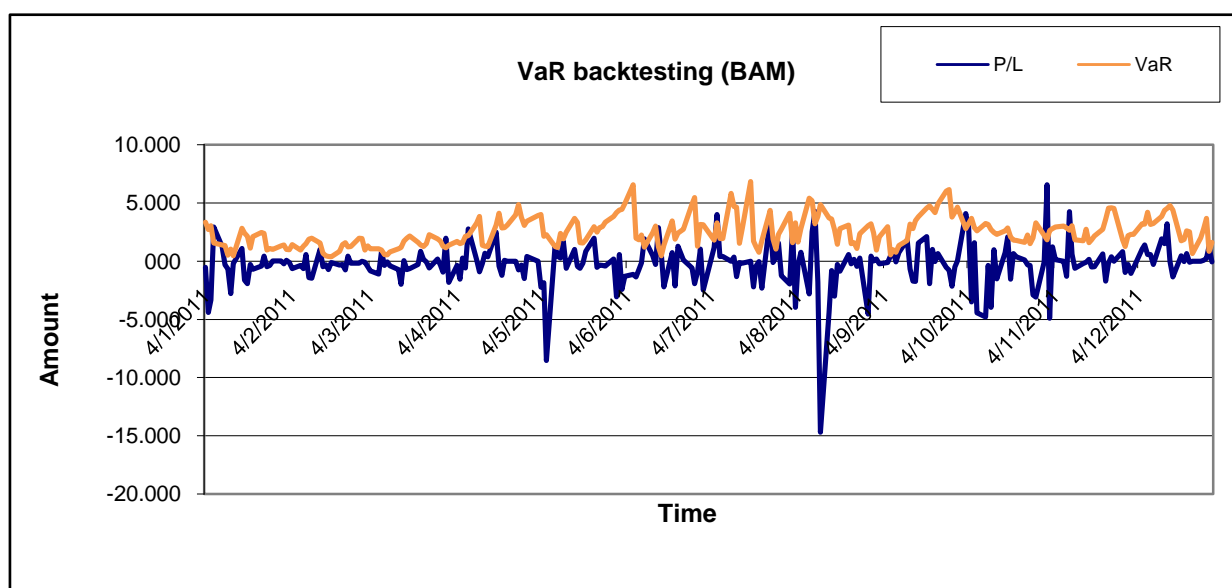
- **Open foreign currency position** – prepared by the Planning and Control Department, checked by the Integrated Risk Management Department, and sent to the Parent Company.
- **Market data:**
- **Local market data** – all local market data unavailable to the Integrated Risk Management Department shall be prepared on a daily basis by the Treasury Division, sent to the Integrated Risk Management Department and to the Parent Company.
- **International market data** – all international market data unavailable to the Integrated Risk Management Department shall be prepared on a daily basis by the Treasury Division, sent to the Integrated Risk Management Department and to the Parent Company.

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33. FINANCIAL INSTRUMENTS (continued)

Financial risk management objectives (continued)

The quality of the implemented risk measurement model must be constantly assessed. Back testing is way to achieve this goal. The essence of back testing procedure is comparing the computed VaR measure with the P&L for the same period. Based on back testing results opinion on the internal model quality shall be created.



During 2011 the Bank recorded twenty for back-testing exceptions (2010: nine exception), when actual losses exceeded daily VARamount.

The Bank is exposed to foreign currency risk when there is no matching between assets and liabilities due to cash flows denominated in foreign currencies. Portfolio exposure to foreign currency risk arises from portfolio sensitivity to fluctuations in exchange rate values. The degree of foreign currency risk depends on the amount of open positions and the degree of potential change in foreign currency rates.

The carrying amounts of the Bank's foreign currency denominated monetary assets and liabilities at the reporting date are as follows:

	Assets		Liabilities	
	31 December 2011	31 December 2010	31 December 2011	31 December 2010
EUR	736,601	820,944	771,713	832,539
USD	18,465	16,658	18,983	16,573
CHF	2,929	2,073	2,761	2,008
HRK	955	1,546	916	1,478
GBP	289	295	283	274
Other	1,133	866	1,164	643

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33. FINANCIAL INSTRUMENTS (continued)

Financial risk management objectives (continued)

The Bank is not exposed to foreign currency risk related to EUR due to the fact that Convertible Mark is pegged to EURO (1 EUR = KM 1,955830). Change in the exchange rate would require the amendments of the law and approval by Parliamentary Assembly of Bosnia and Herzegovina. Exposure is more prominent for USD and CHF. The following table details the Bank's sensitivity to a 10% increase or decrease in foreign currency rates against the relevant local currencies. The sensitivity rate of 10% is used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the reasonably possible change in foreign exchange rates.

31 December 2011

Currency	Open position (in KM)	Stress Test	
		10% Move Up	10% Move Down
CHF	168,000	16,800	(16,800)
GBP	6,000	600	(600)
USD	140,000	14,000	(14,000)
HRK	39,000	3,900	(3,900)
CAD	4,000	400	(400)
AUD	7,000	700	(700)
Other	(42,000)	(4,200)	4,200
EUR	16,459,000	-	-

31 December 2010

Currency	Open position (in KM)	Stress Test	
		10% Move Up	10% Move Down
CHF	65,000	6,500	(6,500)
GBP	21,000	2,100	(2,100)
USD	85,000	8,500	(8,500)
HRK	68,000	6,800	(6,800)
CAD	10,000	1,000	(1,000)
AUD	17,000	1,700	(1,700)
Other	196,000	19,600	(19,600)
EUR	(11,595,000)	-	-

Result of KM thousand profit/loss on USD position at 31 December 2011 is the result of having the Bank open position in USD equal to KM 140,000 (USD assets KM 18,465 thousand and liabilities KM 18,983 thousand). If we take in consideration foreign currency movements and predict 10% positive or negative change applied to an open position of KM 140 thousand, the Bank is exposed to a FX risk in the amount of KM 14 thousand. In case of a long position with a positive market movements the Bank will record a profit and loss in the opposite case.

The analysis outlined above is used on open foreign currency position of the Bank, which includes all asset and liability items.

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33. FINANCIAL INSTRUMENTS (continued)

Financial risk management objectives (continued)

If the currency position of a foreign currency is "long" (assets exceeding liabilities) and the exchange rate for this currency increases in relation to the KM, the Bank will experience a foreign exchange gain.

If the currency position of a foreign currency is "long" (assets exceeding liabilities) and the exchange rate for this currency decreases in relation to the KM, the Bank will experience a foreign exchange loss.

If the currency position of a foreign currency is "short" (liabilities exceeding assets) and the exchange rate for this currency increases in relation to KM, the Bank will experience a foreign exchange loss.

If the currency position of a foreign currency is "short" (liabilities exceeding assets) and the exchange rate for this currency decreases in relation to KM, the Bank will experience a foreign exchange gain.

The Bank takes on exposure to effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Bank monitors its foreign exchange (FX) position for compliance with the regulatory requirements of the Banking Agency of Federation of Bosnia and Herzegovina established in respect of limits on open positions. The Bank seeks to match assets and liabilities denominated in foreign currencies to avoid foreign currency exposures.

Interest rate risk management

The Bank is exposed to interest rate risk as the Bank borrows funds at both fixed and floating interest rates. The risk is managed by the Bank by maintaining an appropriate mix between fixed and floating rate borrowings.

The Bank's exposures to interest rates on financial assets and financial liabilities are detailed in the liquidity risk management section of this note.

Interest rate risk reflects the possibility of loss of profit and/or erosion of capital due to a change in interest rates. It relates to all products and balances that are sensitive to changes in interest rates. This risk comprises two components: income component and investment component.

The income component arises from a lack of harmonization between the active and passive interest rates of the Bank (interest on placements is fixed, interest for liabilities is variable and vice versa).

The investment component is a consequence of the inverted relationship between price and interest rate fluctuations of securities.

The Bank strives to protect itself from interest rate risk by harmonizing the type of interest rate (fixed and variable), currency, related interest rate and the date of interest rate change for all products for which it concludes contracts (which are sensitive to interest rate changes). Any incongruity among the abovementioned elements results in exposure of the Bank to interest rate risk.

The sensitivity analyses below have been determined based on the exposure to interest rates for both derivatives and non-derivative instruments at the balance sheet date. For floating rate liabilities, the analysis is prepared assuming the amount of liability outstanding at the balance sheet date was outstanding for the whole year. A 200 basis point increases or decrease is used when reporting interest rate risk internally to key management personnel and represents management's assessment of the reasonably possible change in interest rates.

If changes in interest rates market moving had been 200 basis points (2.00%) higher/lower and all other variables were held constant, the Bank's profit for the year ended 31 December 2011 with parallel interest rate shock in 200 bps would decrease 2,621 / 2,621 increase (2010: decrease/increase by KM 3,787 thousand). This is mainly attributable to the Bank's exposure to interest rates on its variable rate borrowings.

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33. FINANCIAL INSTRUMENTS (continued)

Credit risk management

The Bank takes on exposure to credit risk which is the risk upon credit approval and when counterparty will be unable to pay amounts in full when due. The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral and corporate and personal guarantees.

Making decision on exposure to credit risk is, according to the Bank's policy, centralised and concentrated in the Credit Committee for the retail and business. Decisions of the Credit Committees are made upon consideration of proposal provided by the Risk Management Department. The terms for approval of each corporate loan are determined individually depending on client type, loan's purpose, estimated credit worthiness and current market situation. Terms of security that accompany each loan are also determined according to a client credit worthiness analysis, type of credit risk exposure, term of the placement as well as the placement amount.

Commitments arising from the issuance of letters of credit, documentary letters of credit, which are written irrevocable undertakings by the Bank on behalf of a customer (mandatory) authorising a third party (beneficiary) to draw drafts on the Bank up to a stipulated amount under specific terms and conditions, are collateralised by the underlying shipments of goods to which they relate and therefore have significantly less risk. Cash requirements under open letters of credit are considerably less than the commitments under issued guarantees or stand-by letters of credit. However, the Bank records provisions against these instruments on the same basis as is applicable to loans.

Commitments to extend credit, undrawn loan commitments, unutilised overdrafts and approved overdraft loans. The primary purpose of commitments to extend credit is to ensure that funds are available to a customer as required. Commitments to extend credit represent unused portions of authorisations to extend credits in the form of loans, guarantees or stand-by letters of credit. Commitments to extend credit issued by the Bank represent issued loan commitments or guarantees, undrawn portions of and approved overdrafts loans. Commitments to extend credit or guarantees issued by the Bank which are contingent upon customers maintaining specific credit standards (including the condition that a customer's solvency does not deteriorate) are revocable commitments. Irrevocable commitments represent undrawn portions of authorised loans and approved overdraft facilities because they result from contractual terms and conditions in the credit agreements.

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33. FINANCIAL INSTRUMENTS (continued)

Credit risk management (continued)

Financial assets

The credit quality of financial assets is managed by the bank using internal credit ratings. The table below shows the credit quality by class of financial assets exposed to the credit risk, based on the bank's internal credit rating system. The amounts presented are gross of impairment allowances.

31 December 2011	Neither past due nor impaired	Past due but not impaired	Individually impaired	Total
Cash and balances with other banks	163,790	-	-	163,790
Obligatory reserve with the Central Bank	71,158	-	-	71,158
Placements with other banks	31,527	-	-	31,527
Loans and advances to customers	898,620	78,748	119,682	1,097,050
Assets available for sale	15,945	-	47	15,992
	1,181,040	78,748	119,729	1,379,517

31 December 2010	Neither past due nor impaired	Past due but not impaired	Individually impaired	Total
Cash and balances with other banks	66,364	-	-	66,364
Obligatory reserve with the Central Bank	97,789	-	-	97,789
Placements with other banks	190,290	-	-	190,290
Loans and advances to customers	787,743	95,181	93,609	976,533
Assets available for sale	999	-	857	1,856
	1,143,185	95,181	94,466	1,332,832

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33. FINANCIAL INSTRUMENTS (continued)

Credit risk management (continued)

Credit exposure and collaterals

Description	Credit risk exposure			
	Loans given	Undrawn loan commitments and unutilized overdrafts	Commitments / Guarantees issued	Fair value of the collateral
Legal entity	647,407	57,631	65,801	770,839
Retail	449,643	53,377	-	503,020
Total	1,097,050	111,008	65,801	1,273,859
31 December 2010 restated				
Legal entity	560,194	32,341	54,358	421,309
Retail	416,339	40,450	-	129,200
Total	976,533	72,791	54,358	550,509

Fair value of the collateral of loans and commitments

	31.12.2011	31.12.2010
Property	12,377	535,761
Deposits	635,542	14,748
	647,919	550,509

The Collateral Policy of the Bank defines the type of collateral, way of estimating fair value of collaterals and procedure for collection of receivable through collaterals. Type of prescribed collaterals and their respective amount are based on evaluation of every client's credit worthiness. Main categories of accepted collaterals are: cash, real estate, movable property and personal guarantees.

The Bank collateral policy defines also the process of recovery of non-performing loans through collaterals in order to decrease credit risk. The property that the Bank acquired through its collection process (land and buildings in the amount of KM 646 thousand; 2010: KM 1,230 thousand) is not shown among the Bank's property plant and equipment but it is recorded in "Other assets" position (Note 22).

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NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011
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33. FINANCIAL INSTRUMENTS (continued)

Credit risk management (continued)

Fair value of the collateral of loans and commitments (continued)

Analysis of past due but not impaired loans by days of delay:

	Gross amount	Past due days			
		Until 30 days	31 – 60 days	61 – 90 days	Over 90 days
31 December 2011					
Legal entities	38,493	36,370	1,295	828	-
Retail	40,255	28,735	9,416	2,101	3
Total	78,748	65,105	10,711	2,929	3

	Gross amount	Past due days			
		Until 30 days	31 – 60 days	61 – 90 days	Over 90 days
31 December 2010					
Legal entities	46,642	39,934	3,966	981	1,761
Retail	48,539	34,496	11,402	2,616	25
Total	95,181	74,430	15,368	3,597	1,786

Renegotiated loans

Where possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment agreements 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 impairment assessment. The amount of renegotiated loans in 2011 was KM 57,293thousand and in 2010was KM 52,737thousand.

Loans and other assets written off and recorded off-balance sheet

According previous FBA regulation the Bank had obligation to record assets fully provisioned in off-balance sheet records. In 2010 movements in loans and other assets written off and recorded off-balance sheet wereas follows:

	Loans and receivables and commitments	Assets available for sale	Other assets	Total
31 December 2009	34,824	857	3,567	39,248
Currency differences and reclassification of beginning balances	2	-	88	90
Write-offs in 2010	14,256	-	246	14,502
Collections	(4,628)	-	(115)	(4,743)
Collections – deferred income	(273)	-	-	(273)
Total write offs	(1,725)	-	(141)	(1,866)
31 December 2010	42,456	857	3,645	46,958

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33. FINANCIAL INSTRUMENTS (continued)

Credit risk management (continued)

Loans and other assets written off and recorded off-balance sheet (continued)

With 31 December 2010 the Bank restated Off balance sheet assets from Off balance to Balance Sheet:

- amounts of Loans and receivables (39,440 thousand KM) and commitments (3,016 thousand KM) are shown in Loans and receivables position (total amount 42,456 thousand KM)
- from the total amount of Other assets classified in E category in 2010 (3,645 thousand KM) the Bank restated amount of 2,970 thousand KM in Balance Sheet. Difference relates to property received in collection process for which the Bank has not indications for selling.
- The amount of Assets available for sale (857 thousand KM) is restated into same position in Balance Sheet.

From 2011 fully provisioned assets is part of Balance Sheet records. In 2011 the Bank did permanent write offs as follows:

	Loans and receivables Note 20	Assets available for sale Note 21	Other assets Note 22	Commitments	Total
Total write offs	2,676	810	362	-	3,848

Liquidity risk management

Liquidity risk is a measure of the extent to which the Bank may be required to raise funds to meet its commitments associated with financial instruments. The Bank maintains its liquidity profiles in accordance with regulations laid down by the Banking Agency of Federation of Bosnia and Herzegovina.

The Bank is exposed to daily calls on its available cash resources from overnight deposits, current accounts, maturing deposits, loan draw downs, guarantees and from margin and other calls on cash-settled derivatives. The Bank does not maintain cash resources to meet all of these needs as experience shows that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty. The Bank sets limits on the minimum proportion of maturing funds available to meet such calls and on the minimum level of interbank and other borrowing facilities that should be in place to cover withdrawals at unexpected levels of demand.

The following tables present in details the Bank's remaining contractual maturity for its financial assets and non-derivative financial liabilities. The tables have been drawn up based on the undiscounted cash flows of financial assets / liabilities based on the earliest date on which the Bank can be required to receive or pay. The table includes both interest and principal cash flows.

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33. FINANCIAL INSTRUMENTS (continued)

Liquidity risk management (continued)

	Less than 1 month	1-3 months	3 months to 1 year	1-5 years	5+ years	Total
31 December 2011						
Cash and balances with Central bank	228,193	-	-	-	-	228,193
Placement with other banks	37,980	-	-	-	-	37,980
Loans and receivables	147,514	80,541	311,895	424,482	231,333	1,195,765
Assets available for sale	-	6,908	8,327	212	-	15,447
Other financial assets	4,510	-	-	-	-	4,510
TOTAL ASSETS	418,196	87,448	320,221	424,694	231,333	1,481,895
31 December 2010						
Cash and balances with Central bank	164,153	-	-	-	-	164,153
Placement with other banks	189,682	-	-	-	1,246	190,928
Loans and receivables	55,783	61,612	292,625	435,996	402,679	1,248,695
Assets available for sale	2	4	19	174	1,557	1,756
Other financial assets	2,465	-	-	-	1,229	3,694
TOTAL ASSETS	412,085	61,616	292,644	436,17	406,711	1,609,226
	Less than 1 month	1-3 months	3 months to 1 year	1-5 years	5+ years	Total
31 December 2011						
Due to banks and other institutions	87,781	1,156	146,995	115,949	57,571	409,452
Subordinated debit	2	44	137	699	287	1,171
Due to customers	380,101	41,173	194,112	157,701	10,541	783,628
Other financial liabilities	8,461	-	-	-	-	8,461
TOTAL LIABILITIES	476,345	42,373	341,244	274,349	68,399	1,202,711
31 December 2010						
Due to banks and other institutions	83,525	28,438	81,383	224,764	66,175	484,285
Subordinated debit	-	40	122	702	561	1,425
Due to customers	380,134	23,266	122,755	171,601	11,944	709,700
Other financial liabilities	2,724	-	-	-	148	2,872
TOTAL LIABILITIES	466,383	51,744	204,260	397,067	78,828	1,198,282

Expected maturities are not expected to defer from the contractual maturities, except in the area of demand deposits which may be extended according to clients' preferences.

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33. FINANCIAL INSTRUMENTS (continued)

Liquidity risk management (continued)

The following tables presents in details the Bank's remaining contractual maturity for its commitments and contingent liabilities

	Less than 1 month	1-3 months	3 months to 1 year	1-5 years	5+ years	Total
31 December 2011						
Guarantees	6,377	13,951	33,093	11,693	115	65,229
Letter of credit	538	34	-	-	-	572
Unused portion of loans	4,823	8,805	82,170	15,210	-	111,008
	11,738	22,790	115,263	26,903	115	176,809
31 December 2010						
Guarantees	2,343	8,195	27,656	9,854	115	48,163
Letter of credit	540	1,517	4,138	-	-	6,195
Unused portion of loans	3,618	8,079	56,935	4,159	-	72,791
	6,501	17,791	88,729	14,013	115	127,149

The following tables details the Bank's commitments and contingent liabilities allocated according to the earliest date they can be drawn:

	Less than 1 month	1-3 months	3 months to 1 year	1-5 years	5+ years	Total
31.12.2011						
Guarantees	9,908	13,114	31,107	10,992	108	65,229
Letter of credit	540	32	-	-	-	572
Unused portion of loans	11,194	8,277	77,240	14,297	-	111,008
	21,642	21,423	108,347	25,289	108	176,809
31.12.2010						
Guarantees	5,550	7,622	25,720	9,164	107	48,163
Letter of credit	936	1,411	3,848	-	-	6,195
Unused portion of loans	8,460	7,513	52,950	3,868	-	72,791
	14,946	16,546	82,518	13,032	107	127,149

The Bank has access to sources of financing with total unused amount of KM 48,972 thousand (2010: KM 86,862 thousand) at the balance sheet date. The Bank expects to meet its other obligations from operating cash flows and proceeds of maturing financial assets.

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34. TAX RISKS

The tax system in Bosnia and Herzegovina is in the process of continuous revisions and changes. There are still, however, different interpretations of tax regulations. In different circumstances, Tax Authorities may have different approaches in certain tax areas and may identify additional tax liabilities and penalty interests. In Bosnia and Herzegovina tax period remains open for a period of five years. Outdating of the right of Tax Authorities to impose taxes, interests and fines is discontinued with every official action of the Tax Authorities to impose and collect taxes. After each of such discontinuation, new outdating period starts and the time before that discontinuation is not included in the legal outdating period. The Management of the Company believes that tax liabilities are correctly presented in these financial statements.

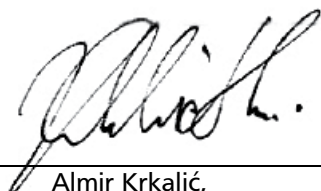
35. EVENTS AFTER THE BALANCE SHEET DATE

No events have occurred since the balance sheet date, which significantly affect the state of affairs of the Bank at the balance sheet date or which require additional disclosure.

36. APPROVAL OF THE FINANCIAL STATEMENTS

These financial statements were approved for issue by the Management Board. The Bank's Supervisory Board and the General Assembly have the power to amend these financial statements after issue.

Approved by and signed on behalf of the Management Board:



Almir Krkalić,
Director



Dario Grassani
Executive director of Finance