AIB Mortgage Bank

Directors' Report & Financial Statements

Year ended 31 December 2009

AIB Mortgage Bank

Directors' report and financial statements

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Directors' and other information

Directors	Maeliosa Ó hOgartaigh (Acting Chairman from 01/09/2009) David Kelly* (Managing Director) Seymour Cresswell* Kieran Crowley Michael Keegan* Walter Brazil (appointed 25/03/2010) Jim Pender* (appointed 21/07/2009) Jennifer Winter * Executive Director
Registered office	Bankcentre Ballsbridge Dublin 4 Ireland
Secretary	David Schorman (appointed 25/03/2010)
Registered Auditor	KPMG Chartered Accountants 1 Harbourmaster Place International Financial Services Centre Dublin 1 Ireland
Solicitor	Bryan Sheridan Group Law Agent Allied Irish Banks, p.l.c. Bankcentre Ballsbridge Dublin 4 Ireland
Banker	Allied Irish Banks, p.l.c.
Cover-Assets Monitor	Mazars Harcourt Centre Block 3 Harcourt Road Dublin 2 Ireland

AIB Mortgage Bank

Directors' Report

The Directors present their report and financial statements for the year ended 31 December 2009. A statement of Directors' responsibilities in relation to the financial statements appears on page 9.

Principal activities

AIB Mortgage Bank ('the Bank'), a public unlimited company, obtained an Irish banking licence under the Irish Central Bank Act, 1971 (as amended) and was registered as a designated mortgage credit institution under the Asset Covered Securities Act, 2001 on 8 February 2006. The Bank is a wholly owned subsidiary of Allied Irish Banks, p.l.c., ('AIB') and is regulated by the Central Bank and Financial Services Authority of Ireland ('CBFSAI'). Its principal purpose is to issue mortgage covered securities for the purpose of financing mortgage loans secured on residential property in accordance with the Asset Covered Securities Act, 2001 and the Asset Covered Securities (Amendment) Act 2007 ('the Asset Covered Securities Acts'). Such mortgage loans may be made directly by the Bank or may be purchased from Allied Irish Banks, p.l.c. and other subsidiary undertakings of AIB Group or third parties.

The Bank commenced trading on 13 February 2006, when Allied Irish Banks, p.l.c. transferred its Republic of Ireland branch originated residential mortgage business, amounting to €13.6bn in mortgage loans, to AIB Mortgage Bank; certain other categories of Allied Irish Banks, p.l.c. residential mortgage loans were not included in this transfer. On 24 February 2006, a Mortgage-Backed Promissory Note facility between AIB Mortgage Bank and the Central Bank and Financial Services Authority of Ireland was put in place. In March 2006, the Bank launched a €15bn Mortgage Covered Securities Programme (the 'Programme') and has launched a number of covered bond issues since that date. The Programme was subsequently increased in 2009 to €20bn.

The Bank's business activities are restricted, under the Asset Covered Securities Acts, to dealing in, and holding, mortgage credit assets and limited classes of other assets, engaging in activities connected with the financing and refinancing of such assets, entering into certain hedging contracts and engaging in other activities which are incidental to or ancillary to the above activities.

Most of the Bank's activities are outsourced to Allied Irish Banks, p.l.c. under an Outsourcing and Agency Agreement. Allied Irish Banks, p.l.c., as Service Agent for the Bank, originates residential mortgage loans through its retail branch network in the Republic of Ireland, services the mortgage loans, provides treasury services in connection with financing as well as a range of other support services.

The Bank's activities are financed through the issuance of mortgage covered securities and a Mortgage-Backed Promissory Note facility with the Central Bank and Financial Services Authority of Ireland, with the balance of funding being provided by Allied Irish Banks, p.l.c.

Governance is exercised through a Board of Directors, comprising normally, except in periods during which replacement appointments are pending, five executive Directors and two non executive Directors all of whom are AIB employees. Two of the non executive Directors are independent non executive directors of Allied Irish Banks, p.l.c.

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

Business review

Since August 2007, global financial markets have experienced significant volatility and turmoil which have caused a breakdown of wholesale banking markets, large write-downs of financial assets by financial institutions, a major change in the banking landscape and a credit crunch leading to serious problems for the non-financial sectors.

Following several years of strong economic growth, Ireland officially went into recession in 2008. During 2009, the recession deepened with Irish GDP estimated to have declined by approximately 7.1%. There was a fall in total employment and an increase in unemployment to 12.5% at December 2009, although the pace of increase is now moderating. Housing output fell by over 25% from 2008 and there have been substantial falls in house sales activity and in house prices.

Directors' Report

Business review *(continued)*
AIB is currently one of the few financial institutions offering competitive home loans in the Irish market. Our main focus is first-time buyers, although we are also keen to support existing customers who want to trade up their property or top up their mortgage.

AIB adheres to various Irish statutory and voluntary guidelines which protect family homes. These guidelines include the Code of Conduct on Mortgage Arrears, the Irish Banking Federation ('IBF')/Money Advice & Budgeting Service protocol and the IBF Statement of Intent.

Total market mortgage drawdowns by value in Ireland were significantly lower than in 2008 and the Bank's mortgage drawdowns were also lower, but fell less than the total market drawdowns.

Total impaired loans, €381.7m, increased to 1.84% of total loans (2008 €134.5m or 0.67%). Provisions made for impaired loans in 2009 increased to €78.7m from €27.2m in 2008. As a result of the deterioration in the economy and the additional pressure on borrowers, AIB has applied additional resources to its credit management function.

Net interest income has increased in 2009, mainly because the one month Euribor rate (the basis for most of the Bank's funding) was on average 0.33% below the ECB Refi rate (the basis for most of the Bank's customer pricing) in 2009 whereas it was on average 0.44% above it in 2008. This level of net interest income is not considered sustainable, as the one month Euribor rate is expected to increase relative to the ECB Refi rate and as covered bond issuances to external investors are expected to carry a higher interest cost.

Certain mortgage loans connected to property developers will be transferred during 2010 to the National Asset Management Agency (NAMA) in accordance with the terms and timelines prescribed by NAMA. In respect of the actual transfer process, assets to be transferred to NAMA from AIB Mortgage Bank will firstly transfer from AIB Mortgage Bank to Allied Irish Banks, p.l.c. at fair value for onward transfer to NAMA. The fair value attaching to the transferred assets will be based on the valuation NAMA place on the transferred assets. Further information is given in Note 14 to the financial statements.

Results for the year
Profit before taxation for 2009 was €94.3m, up from €1.3m in 2008, due mainly to the increase in net interest income, reduced by an increase in provisions for impaired loans.

Net interest income was €217.6m compared with €81.5m in 2008. Interest margins were higher mainly due to lower funding costs for reasons stated above. This reduction in funding costs was partially offset by higher liquidity premium costs, and higher maturity transformation costs, being the cost of transforming borrowing for periods longer than one month back to one month for interest matching.

Interest income on mortgage loans was €528.5m (2008: €935.4m), the decrease being largely due to a decrease in market interest rates. Interest rates charged on owner occupier loans were not increased in 2009. Interest income from deposits and interest rate swaps with Allied Irish Banks, p.l.c. was €364.2m (2008: €610.5m), the decrease resulting mainly from a decline in one month Euribor interest rate on funds placed with Allied Irish Banks, p.l.c.

Interest payable to Allied Irish Banks, p.l.c. on deposits and on interest rate swaps was €341.3m (2008: €990.6m), the decrease being due to the lower one month Euribor interest rates. Interest payable to the Central Bank and Financial Services Authority of Ireland in respect of the Mortgage-Backed Promissory Note facility was €32.1m (2008: €25.1m) due mainly to higher usage of the facility offset by falling interest rates. Interest payable to holders of mortgage covered securities was €301.7m (2008: €448.7m), mainly due to lower ECB Refi and one month Euribor interest rates and the redemption of a €2.5bn bond on 30 April 2009.

Directors' Report

Results for the year *(continued)*
The provisions charge for impaired loans in 2009 was €78.7m, up from €27.2m in 2008. Provisions as at 31 December 2009 which excludes assets held for sale amounted to €116.2m of which €67.7m were specific and €48.5m were Incurred But Not Reported ("IBNR").

Changes in the fair value of interest rate swaps, and certain related account items being hedged, resulted in a mark to market loss of €1.5m (2008: €11.4m).

Administrative expenses amounted to €36.1m (2008: €39.9m), and included €33.2m (2008: €36.8m) for services provided by Allied Irish Banks, p.l.c. under the Outsourcing and Agency Agreement.

Profit after taxation amounted to €82.5m (2008: €1.1m).

Mortgage Loan Portfolio
While drawdowns of mortgages were lower than the previous year, the Bank's mortgage portfolio grew by 3.5% during 2009 to €20.7bn as at 31 December 2009 (2008: 8.5%)

Funding activities
In 2009, the European covered bonds market began to recover from the widespread disruption to its normal activities. This was assisted by the ECB purchase programme announced in May. Gross new issuance of Euro benchmark covered bonds was higher in 2009 than in 2008. The Irish covered bond market re-opened in the fourth quarter of 2009 with two Irish mortgage providers issuing benchmark bonds to external investors. At present, however, new issuance of bonds by Irish banks, in common with banks in a number of financially weaker jurisdictions, carry a funding cost premium.

During the year the Bank did not raise new covered bond funding from external investors under the Programme. On 30 April 2009, the Bank redeemed its inaugural 3 year €2.5bn bond issued on 5 April 2006. In order to augment AIB's liquidity surplus and contingent funding capacity, the Bank completed self issuances to itself, AIB Mortgage Bank. A €2.5bn Irish government guaranteed bond was issued on 30 April 2009, and was redeemed early on 27 November 2009. Following this, a 7 year €2.5bn non government guaranteed bond was issued on 10 December 2009. In addition, a €1bn 5 year non government guaranteed self issuance was made on 28 September 2009.

The Bank also undertook two small issuances of registered covered bonds outside of the Programme comprising of a €15m 10 year public issue on 23 September 2009 and a €50m 10 year public issue on 30 September 2009.

At 31 December 2009, total covered bonds in issue amounted to €14.0bn (2008: €13.0bn), of which €4.7bn was issued to external investors, €5.8bn was issued to Allied Irish Banks, p.l.c. and €3.5bn was self issued to AIB Mortgage Bank. See note 17 for details.

At 31 December 2009, a €1.5bn self issuance bond was used to provide liquidity through a sale and repurchase agreement with the ECB which matures on 23 December 2010.

Following the redemption on 29 January 2010 of the 3 year €2bn bond, none of the principal due on the remaining covered bonds in issue is covered by the government guarantee scheme, as they fall due for payment after the expiry of the guarantee on 29 September 2010.

The Mortgage-Backed Promissory Note facility with the Central Bank was used as a source of liquidity during the year but at 31 December 2009, none of it was drawn (31 December 2008, nil drawn).

AIB Mortgage Bank

Directors' Report

Risks and uncertainties
Information concerning the principal risks and uncertainties facing the Bank as required under the terms of the European Accounts Modernisation Directive (2003/51/EEC) is set out in Note 8 to the Financial Statements.

Share capital
The share capital of the Bank was €450m, being ordinary shares of €1 each, as at 31 December 2009.

Capital resources and regulatory capital ratios
The table below shows the components of the AIB Mortgage Bank's Tier 1 and total capital ratios as at 31 December 2009 and 31 December 2008.

	CRD 31 Dec 2009 €'000	CRD 31Dec 2008 €'000
Tier 1		
Paid up ordinary share capital	**450,000**	450,000
Eligible reserves	**119,868**	87,648
Total tier 1 capital	**569,868**	537,648
Tier 2		
Subordinated perpetual loan capital	**200,000**	200,000
Subordinated term loan capital	**100,000**	100,000
IBNR (standardised amount)	**1,784**	-
Total tier 2 capital	**301,784**	300,000
Gross capital		
Supervisory deductions	**(77,115)**	(39,275)
Total capital	**794,537**	798,373
Risk weighted assets		
On balance sheet	**4,948,340**	5,851,759
Off-balance sheet *	**62,010**	67,954
Total risk weighted assets	**5,010,350**	5,919,713
Capital ratios		
Tier 1	**10.98%**	8.81%
Total	**15.31%**	13.08%

The capital ratios are calculated in accordance with Pillar I of the Capital Requirements Directive ("CRD") and are presented above before the application of Transitional Arrangements required for reporting to the Financial Regulator. For 2009, the Transitional Arrangements require banks, on a rolling basis, to maintain minimum capital requirements equal to 95% of their pre-CRD Capital Requirements. When applied, the minimum requirement generates a Total Capital Ratio of 8.6% as at 31 December 2009 (2008: 8.5%).

* See Note 29 to the financial statements for approved but undrawn mortgage loans, weighted at 7% under the CRD.

Directors' Report

Outlook
We expect the operating environment to remain difficult for the foreseeable future.

Books of account
The measures taken by the Directors to secure compliance with the Bank's obligation to keep proper books of account are the use of appropriate systems and procedures and the employment of competent persons. The books of account of the Bank are kept at the Bank's registered office.

Going concern
The Mortgage Bank's activities are subject to risk factors. The continued global financial crisis and the deteriorated economic environment in which it operates has increased the intensity of these risk factors. The principal risks that the Bank faces, which the Directors have considered in the context of continuing as a going concern, are described on pages 29 to 39. AIB Mortgage Bank is also dependent on its Parent, Allied Irish Banks, p.l.c. for continued funding and is therefore dependent on the going concern status of the Parent.

Allied Irish Banks, p.l.c's Directors have reviewed the AIB Group's Business and Financial Plan for 2010/2011 which incorporates its funding and capital plan and have considered the critical assumptions underpinning same. They have also considered the measures introduced by the Irish Government to improve liquidity, including the Government Guarantee, the €3.5 billion recapitalisation, AIB's participation in NAMA and its acknowledgement of AIB's systemic importance to the Irish economy. The financial statements of Allied Irish Banks, p.l.c. continue to be prepared on a going concern basis, as the Directors are satisfied that the Group as a whole have access to the resources to continue in business for the foreseeable future.

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

Directors
The Directors and Secretary of the Bank are set out on page 1.

Directors' and Secretary's interests in shares
The beneficial interests of the Directors and the Secretary in office at 31 December 2009 and of their spouses and minor children in the shares of group companies are set out below. The shares referred to are €0.32 ordinary shares in Allied Irish Banks, p.l.c., the holding company.

Ordinary shares	**31 December 2009**	1 January 2009*
Directors:		
Seymour Cresswell	**1,808**	1,808
Kieran Crowley	**12,520**	12,520
Michael Keegan	**5,645**	5,645
David Kelly	**68,841**	68,520
Gerry O'Connor	**39,738**	38,448
Maeliosa Ó hOgartaigh	**11,329**	11,329
Jim Pender	**26,867**	26,867
Jennifer Winter	**480**	480
Secretary:		
Aidan Maher	**3,920**	3,920

** or later date of appointment*

AIB Mortgage Bank

Directors' Report

Share options
Details of the Directors' and the Secretary's options to subscribe for ordinary shares in Allied Irish Banks, p.l.c., are given below. The vesting of these options to the individuals concerned is dependent on Earnings Per Share ("EPS") targets being met by AIB. Subject thereto, the options outstanding at 31 December 2009 are exercisable at various dates between 2010 and 2015. Details are shown in the Register of Directors' and Secretary's Interests, which may be inspected at the Bank's registered office.

	31 December 2009	1 January 2009	Since 1 January, 2009 Granted	Since 1 January, 2009 Exercised	Price of options exercised	Market price at date of exercise	Weighted average subscription price of options outstanding at 31 December 2009
Directors:					€	€	€
Seymour Cresswell	**-**	-	-	-	-	-	-
Michael Keegan	**22,500**	22,500	-	-	-	-	13.24
David Kelly	**25,000**	25,000	-	-	-	-	14.08
Gerry O'Connor	**-**	-	-	-	-	-	-
Maeliosa Ó'hOgartaigh	**43,000**	43,000	-	-	-	-	13.68
Jim Pender	**-**	-	-	-	-	-	-
Secretary:							
Aidan Maher	-	-	-	-	-	-	-

Non-executive directors do not participate in the share option plans.

Long term incentive plans
Details of the Directors' and the Secretary's conditional grants of awards of ordinary shares are given below. These conditional awards are subject to onerous performance targets being met by AIB, in terms of EPS growth and total shareholder return. In that regard, it was determined by the AIB Remuneration Committee during 2009 that the conditional awards made in 2006 had not met the related performance targets, and, accordingly, that they should lapse – see below. The conditional grants of awards outstanding at 31 December 2009 may wholly or partly vest between 2010 and 2011, depending on the date of the grant and the grant conditions being met.

	Total as at 31 December 2009	Lapsed during 2009	Granted during 2009	Total as at 1 January 2009*
Directors				
Seymour Cresswell	**-**	-	-	-
Michael Keegan	**25,694**	8,116	-	33,810
David Kelly	**27,915**	10,989	-	38,904
Gerry O'Connor	**4,774**	5,452	-	10,226
Maeliosa Ó hOgartaigh	**34,086**	12,035	-	46,121
Jim Pender	**29,106**	10,465	-	39,571
Secretary:				
Aidan Maher	**-**	-	-	-

*or date of appointment, if later.

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

There were no changes in the Directors' and Secretary's interests between 31 December 2009 and 27 March 2010 save for the receipt by Mr. Gerry O'Connor of 204 shares under the Allied Irish Banks, p.l.c. UK Share Ownership Plan up to the date of his resignation. Mr. Walter Brazil was appointed to the Board on 25 March 2010. His interest (inclusive of the interests of his spouse and minor children) in the ordinary shares of Allied Irish Banks p.l.c. is 5,583.

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Directors' Report

Directors and Secretary
Mr. John O'Donnell retired as chairman and as Executive Director on 31 August 2009.
Mr. David Griffin retired as an Executive Director on 21 July 2009.
Mr. Jim Pender was appointed Executive Director on 21 July 2009.
Mr. Gerry O'Connor resigned as an Executive Director on 4 March 2010.
Mr. Walter Brazil was appointed Non Executive Director on 25 March 2010.
Ms. Tanya Barry resigned as Secretary on 21 July 2009 and was replaced on that day by Mr. Aidan Maher.
Mr. Aidan Maher resigned as Secretary on 25 March 2010 and was replaced on that day by Mr. David Schorman.

Post balance sheet events
No significant events that have occurred in the period subsequent to the year end date and the date of approving the financial statements.

Independent auditor
The auditor, KPMG, Chartered Accountants, have signified their willingness to continue in office under Section 160 (2) of the Companies Act, 1963.

On behalf of the Board

Chairman Maelíosa ÓhÓgartaigh

Managing Director David Kelly

25 March 2010

Statement of Directors' responsibilities in relation to the Financial Statements

The Companies Acts require the Directors to prepare financial statements for each financial year. Under the Acts the Directors are required to prepare the financial statements in accordance with International Financial Reporting Standards ('IFRS') as adopted by the EU and applicable law.

The financial statements are required by law and IFRS to present fairly the financial position and performance of the Bank; the Companies Acts provide in relation to such financial statements that references to financial statements giving a true and fair view are references to their achieving a fair presentation.

In preparing the Bank's financial statements, the Directors are required to:

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

The Directors are responsible for keeping proper books of account that disclose with reasonable accuracy at any time the financial position of the Bank and enable them to ensure that its financial statements comply with the Companies Acts 1963 to 2009 and the Asset Covered Securities Acts. They are also responsible for taking such steps as are reasonably open to them to safeguard the assets of the Bank and to prevent and detect fraud and other irregularities.

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

The Directors are also responsible for preparing a Directors' Report that complies with the requirements of the Companies Acts 1963 to 2009.

On behalf of the Board

Chairman Maelíosa ÓhÓgartaigh

Managing Director David Kelly

25 March 2010

Independent auditor's report to the members of AIB Mortgage Bank

We have audited the financial statements of AIB Mortgage Bank ('the Bank') or ("Company") for the year ended 31 December 2009 which comprise the Income Statement, the Statement of Financial Position, the Statement of Cash Flows, the Statement of Comprehensive Income, Statement of Changes in Equity and the related notes. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the Company's members, as a body, in accordance with section 193 of the Companies Act 1990.

Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and auditor

The Directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRS) as adopted by the EU are set out in the Statement of Directors' Responsibilities on page 9.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view in accordance with IFRS as adopted by the EU and have been properly prepared in accordance with the Companies Acts 1963 to 2009.

We also report to you whether, in our opinion:
- proper books of account have been kept by the Bank;
- whether at the reporting date, there exists a financial situation requiring the convening of an extraordinary general meeting of the Bank; and
- whether the information given in the Directors' Report is consistent with the financial statements.

In addition, we state whether we have obtained all the information and explanations necessary for the purposes of our audit, and whether the Bank's Statement of Financial Position is in agreement with the books of account. We also report to you if, in our opinion, any information specified by law regarding Directors' remuneration and Directors' transactions is not disclosed and, where practicable, include such information in our report.

We read the other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. The other information comprises only the Directors' Report. We consider the implications for our report if we become aware of any apparent mis-statements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements.

Basis of audit opinion *(continued)*

It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free of material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion:

• the financial statements give a true and fair view, in accordance with IFRS's as adopted by the EU, of the state of the Bank's affairs as at 31 December 2009 and of its profit for the year then ended; and

• the financial statements have been properly prepared in accordance with the Companies Acts 1963 to 2009.

We have obtained all the information and explanations which we consider necessary for the purposes of our audit. In our opinion proper books of account have been kept by the Bank. The Bank's Statement of Financial Position is in agreement with the books of account.

In our opinion the information given in the Directors' Report is consistent with the financial statements.

The net assets of the Bank, as stated in the Statement of Financial Position are more than half of the amount of its called-up share capital and, in our opinion, on that basis there did not exist at 31 December 2009 a financial situation which under Section 40 (1) of the Companies (Amendment) Act, 1983 would require the convening of an extraordinary general meeting of the Bank.

KPMG

KPMG *25 March 2010*
Registered Auditor
Chartered Accountants
1 Harbourmaster Place
International Financial Services Centre
Dublin 1

(a) The maintenance and integrity of the website on which the AIB Mortgage Bank financial statements are included is the responsibility of the Directors; the work carried out by the auditor does not involve consideration of these matters and, accordingly, the auditor accept no responsibility for any changes that may have occurred to the financial statements or audit report since they were initially presented on the website.

(b) Legislation in the Republic of Ireland governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Accounting policies

The accounting policies applied in the preparation of the financial statements for the year ended 31 December 2009 are set out below. There are no significant changes to the accounting policies described on pages 10 to 16 in the 2008 Annual Report.

1. Reporting entity
AIB Mortgage Bank ('the Bank') is a public unlimited company operating under the Irish Central Bank Act, 1971 (as amended) and as a designated mortgage credit institution under the Asset Covered Securities Acts. It is a wholly owned subsidiary of Allied Irish Banks, p.l.c. and is regulated by the Central Bank and Financial Services Authority of Ireland. Its principal purpose is to issue Mortgage Covered Securities for the purpose of financing loans secured on residential property in accordance with the Asset Covered Securities Acts. Such loans may be made directly by the Bank to customers through the AIB Group branch network in the Republic of Ireland or may be purchased from Allied Irish Banks, p.l.c. and other members of the group or third parties.

2. Statement of compliance
The financial statements have been prepared in accordance with International Accounting Standards and International Financial Reporting Standards (collectively 'IFRS') as issued by the International Accounting Standards Board ("IASB") and adopted by the European Union ("EU") and applicable for the year ended 31 December 2009. The financial statements also comply with the requirements of Irish Statute comprising the Companies Acts 1963 to 2009, the Asset Covered Securities Acts and the European Communities (Credit Institutions: Accounts) Regulations, 1992 as amended by the European Communities (International Financial Reporting Standards and Miscellaneous Amendments) Regulations 2005.

3. Basis of preparation
The financial statements are presented in euro, which is the functional currency of the Bank, rounded to the nearest thousand.

They have been prepared under the historical cost basis, with the exception of the following assets and liabilities which are stated at their fair value: derivative financial instruments, financial instruments at fair value through profit or loss and certain hedged financial liabilities.

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

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and reported amounts of certain assets, liabilities, revenues, expenses and disclosures of contingent assets and liabilities. The estimates and assumptions are based on historical experience and various other factors that are believed to be reasonable under these circumstances. Since management's judgement involves making estimates concerning the likelihood of future events, the actual results could differ from those estimates. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future period affected. The estimates that have a significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are in the areas of impairment of financial assets and fair value of certain financial assets and liabilities. A description of these estimates and judgements is set out within item 17 of this section.

Comparative figures have been adjusted where necessary as a result of changes in accounting policies or to conform with changes in presentation where additional analysis has been provided in the current year.

Accounting policies

3. Basis of preparation *(continued)*

Going Concern

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

Allied Irish Banks, p.l.c's Directors have reviewed the AIB Group's Business and Financial Plan for 2010/2011 which incorporates its funding and capital plan and have considered the critical assumptions underpinning same. They have also considered the measures introduced by the Irish Government to improve liquidity, including the Government Guarantee, the €3.5 billion recapitalisation, AIB's participation in NAMA and its acknowledgement of AIB's systemic importance to the Irish economy. The financial statements of Allied Irish Banks, p.l.c continue to be prepared on a going concern basis, as the Directors are satisfied that the Group as a whole have access to the resources to continue in business for the foreseeable future.

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

Adoption of new accounting standards

The following standards/amendments to standards have been adopted by the Bank during the year ended 31 December 2009:

<u>IFRS 8 – Operating Segments</u>

This standard is effective from 1 January 2009, replacing IAS 14 – Segmental Reporting. IFRS 8 requires operating segments to be identified on the basis of internal reports about components of the entity that are regularly reviewed by the chief operating decision maker in order to allocate resources to the segment and to assess its performance. The introduction of this standard has not had a significant impact on the Bank's reporting.

<u>Revised IAS 1 – Presentation of Financial Statements</u>

This revised standard, effective from 1 January 2009 is aimed at improving users' ability to analyse and compare the information given in financial statements. The revisions include changes in the titles of some of the primary financial statements to reflect their function more clearly. The Bank has adopted the 'two separate statements approach' of presenting items of income and expense and components of other comprehensive income. The revised standard requires all changes in equity arising from transactions with owners in their capacity as owners to be presented separately from non-owner changes in equity in the 'Statement of changes in equity'. Comparative information has been re-presented in accordance with the requirements of the revised standard.

<u>Improving Disclosures about Financial Instruments (Amendments to IFRS 7)</u>

This amended standard, effective for accounting periods commencing on or after 1 January 2009, requires enhanced disclosures about fair value measurements and liquidity risk in respect of financial instruments.

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

Accounting Policies

3. Basis of preparation *(continued)*

Improving Disclosures about Financial Instruments (Amendments to IFRS 7) *(continued)*

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

IAS 32 – Financial Instruments: Presentation and IAS 1 Presentation of Financial Statements – Puttable financial instruments and obligations arising on liquidation

Effective 1 January 2009, the Bank has implemented amendments to IAS 32 Financial Instruments: Presentation and IAS 1 Presentation of Financial Statements. The amendments are relevant to entities that have issued financial instruments that are (i) puttable financial instruments, or (ii) instruments, or components of instruments that impose on the entity an obligation to deliver to another party a pro-rata share of the net assets of the entity only on liquidation. Under the revised IAS 32, subject to specified criteria being met, these instruments will be classified as equity whereas, prior to these amendments, they would have been classified as financial liabilities. The application of the amended requirement did not have any impact on the Bank's financial statements.

4. Interest income and expense recognition

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

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

In calculating the effective interest rate, the Bank estimates cash flows (using projections based on its experience of customers' behaviour) considering all contractual terms of the financial instrument but excluding future credit losses.

The calculation takes into account all fees, including those for early redemption, between parties to the contract that are an integral part of the effective interest rate and all other premiums and discounts.

All costs associated with mortgage incentive schemes including reduced introductory rates and 'cash back' incentives are included in the effective interest calculation.

5. Fee and commission income

Fees and commissions are generally recognised on an accruals basis when the service has been provided unless included in the effective interest rate calculation.

6. Net trading income

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

Accounting policies

7. Financial assets
Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted on an active market and which are not classified as available for sale. They arise when the Bank provides money or services directly to a customer with no intention of trading the loan. Loans are recognised when cash is advanced to the borrowers. Financial assets are initially recognised at fair value and are subsequently carried on an amortised cost basis.

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

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

Financial liabilities are initially recognised at fair value, being the issue proceeds (fair value of consideration received) net of transaction costs incurred. Financial liabilities are subsequently measured at amortised cost, any difference between the proceeds net of transaction costs and the redemption value is recognised in the income statement using the effective interest rate method. Refer to derivatives and hedge accounting, set out within item 9 of this section, for the accounting policy for financial liabilities in a hedge accounting relationship.

9. Derivatives and hedge accounting
Derivatives, such as interest rate swaps, are used only for risk management purposes.

Derivatives
Derivatives are measured initially at fair value on the date on which the derivative contract is entered into and subsequently remeasured at fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and valuation techniques, and discounted cash flow models and options pricing models as appropriate. Derivatives are included in assets when their fair value is positive and in liabilities when their fair value is negative, unless there is the legal ability and intention to settle net. Profits or losses are only recognised on initial recognition of derivatives when there are observable current market transactions or valuation techniques that are based on observable market inputs.

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

Hedging
All derivatives are carried at fair value in the Statement of Financial Position and the accounting treatment of the resulting fair value gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. Where derivatives are held for risk management purposes, and when transactions meet the criteria specified in IAS 39 “Financial Instruments: Recognition and Measurement”, the Bank designates certain derivatives as hedges of the fair value of recognised assets or liabilities or firm commitments (fair value hedge).

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

Accounting policies

9. Derivatives and hedge accounting *(continued)*
The Bank discontinues hedge accounting when:
(a) it is determined that a derivative is not, or has ceased to be, highly effective as a hedge;
(b) the derivative expires, or is sold, terminated, or exercised; and
(c) the hedge item matures or is sold or repaid.

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

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

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

Derivatives used to manage interest rate risk arising on mortgage covered securities have been designated as fair value hedges.

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

Derivatives used to manage interest rate risk arising on mortgage loans to customers do not qualify for hedge accounting. Changes in their fair value are recognised immediately in the income statement.

10. Non-current assets held for sale
A non-current asset or a group of assets containing a non-current asset (a disposal group) is classified as held for sale if its carrying amount will be recovered principally through sale rather than through continuing use, it is available for immediate sale and sale is highly probable within one year. For the sale to be highly probable, the appropriate level of management must be committed to a plan to sell the asset.

On initial classification as held for sale, non-current assets and disposal groups are measured at the lower of their previous carrying amount and fair value less costs to sell with any adjustments taken to the Income Statement. The same applies to gains and losses on subsequent remeasurement. However, financial assets within the scope of IAS 39 continue to be measured in accordance with that standard. No reclassifications are made in respect of prior periods.

Impairment losses subsequent to classification of assets as held for sale are recognised in the Income Statement. Increases in fair value less costs to sell of assets that have been classified as held for sale are recognised in the Income Statement to the extent that the increase is not in excess of any cumulative impairment loss previously recognised in respect of the asset. Assets are not depreciated while they are classified as held for sale.

Accounting policies

11. Financial assets held for sale to NAMA
Assets that the Bank believes will be transferred to NAMA are classified as financial assets held for sale to NAMA in the Statement of Financial Position. These assets are measured on the same basis as prior to their classification as held for sale (see accounting policy number 10). Interest income and fee income for such assets are recognised on the same basis as for loans and receivables and will be recognised up to the date of derecognition (see accounting policy number 5). The impairment policy for loans and receivables as set out in accounting policy number 12 continues to apply.

Derecognition will take place on a date specified by NAMA for the legal transfer of the assets which will also be the date on which the risks and rewards inherent in these assets will transfer. The consideration received will be measured at fair value. The difference between the carrying value at the date of derecognition and consideration received will be recognised in the Income Statement as a gain or loss in other operating income.

In respect of the actual transfer process, assets to be transferred to NAMA from AIB Mortgage Bank will firstly transfer from AIB Mortgage Bank to Allied Irish Banks, p.l.c. at fair value for onward transfer to NAMA. The fair value attaching to the transferred assets will be based on the valuation NAMA place on the transferred assets.

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

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

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

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

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

Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

Accounting policies

12. Impairment of financial assets *(continued)*
For loans and receivables, the amount of impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate. The amount of the loss is recognised using an allowance account and the amount of the loss is charged to the Income Statement. When a loan has been subject to a specific provision and there is no more than a remote likelihood of recovery of such amount, the amount is written off against the related provision for loan impairment. Subsequent recoveries of amounts previously written off decrease the amount of the provision for loan impairment in the income statement.

13. Employee benefits
Retirement benefit obligations
The Bank provides employees with post retirement benefits mainly in the form of pensions. It is AIB Group policy to provide for pension and other post-retirement benefits at rates recommended by independent actuaries. Staff members of the Bank are members of defined benefit or defined contribution schemes administered by Allied Irish Banks, p.l.c.

AIB's defined benefit scheme was closed to new members from December 1997. Employees who joined AIB since December 1997 joined on a defined contribution basis. In December 2007, the Group introduced a hybrid pension arrangement for employees in the Republic of Ireland who are not members of the defined benefit scheme. This arrangement includes elements of both a defined benefit and a defined contribution scheme. It is not possible to identify the Bank's share of the underlying assets and liabilities of the main scheme. Consequently, the main scheme is accounted for as a defined contribution scheme. The standard contribution rate in Ireland was 8% for 2007 and increased to 10% in respect of the defined contribution elements of the hybrid arrangement.

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

15. Taxation
Income tax comprising current tax is recognised in the Income Statement. Current tax is the expected tax payable on the taxable income for the year using tax rates enacted or substantively enacted at the reporting date and any adjustment to tax payable in respect of previous years. Income tax payable on profits based on the applicable tax law is recognised as an expense in the period in which the profits arise.

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

17. Accounting estimates and judgements
The estimates that have a significant impact on the financial statements and estimates with a significant risk of material adjustment in the next year are set out below:

(a) Loan impairment
The estimation of potential loan losses is inherently uncertain and depends upon many factors, including loan loss trends, portfolio grade profiles, local and international economic climates and other external factors such as legal and regulatory requirements. For example, should the expectation of loss within a portfolio increase, then this may result in an increase to the required incurred but not reported ('IBNR') loan loss provision level.

A specific provision is made against problem loans when, in the judgement of management, the estimated repayment realisable from the obligor, including the value of any security available, is likely to fall short of the amount of principal and interest outstanding on the obligor's loan account.

Accounting policies

17. Accounting estimates and judgements *(continued)*

(a) Loan impairment (continued)

The amount of the specific provision made in the Bank's financial statements is intended to cover the difference between the assets carrying value and the present value of estimated future cash flows discounted at the assets original effective interest rates. The management process for the identification of loans requiring provision is underpinned by independent tiers of review.

Credit quality and loan loss provisioning are independently monitored by management on a regular basis. A system for grading advances according to agreed credit criteria exists with an important objective being the timely identification of vulnerable loans so that remedial action can be taken at the earliest opportunity. Credit rating is fundamental to the determination of provisioning in the Bank; it triggers the process which results in the creation of a specific provision on individual loans where there is doubt on recoverability.

IBNR provisions are also maintained to cover loans, which are impaired at the reporting date and, while not specifically identified, are known from experience to be present in any portfolio of loans.

IBNR provisions are maintained at levels that are deemed appropriate by management having considered: credit grading profiles and grading movements, historic loan loss rates, changes in credit management, procedures, processes and policies, levels of credit management skills, local and international economic climates, portfolio sector profiles and current estimates of expected loss in the portfolio.

Estimates of expected loss are driven by the following key factors;

(a) Probability of default i.e. the likelihood of a customer defaulting on its obligations over the next 12 months,

(b) Loss given default i.e. the fraction of the exposure amount that will be lost in the event of default, and

(c) Exposure at default i.e. exposure is calculated by adding the expected drawn balance plus a percentage of the unused limits.

AIB's rating systems have been internally developed and are continually being enhanced, e.g. externally benchmarked, to help underpin the aforementioned factors which determine the estimates of expected loss. Estimated expected loss is only one element in assessing the adequacy of the Bank's allowances.

Provisions and provision adequacy are approved on a quarterly basis. These provisions are in turn reviewed and approved by the AIB Republic of Ireland Division on a quarterly basis with ultimate levels being approved by the AIB Mortgage Bank Audit Committee and the AIB Mortgage Bank Board of Directors.

(b) Fair value of financial instruments

The Bank's financial instruments, which include derivatives, are carried at fair value. Financial instruments are either priced with reference to a quoted market price for that instrument or by using a valuation model. Where the fair value is calculated using financial-markets pricing models, the methodology is to calculate the expected cash flows under the terms of each specific contract and then discount these values back to a present value. These models use as their basis independently sourced market parameters including, for example, interest rate yield curves. The valuation model used for a particular instrument, the quality and liquidity of market data used for pricing, other fair value adjustments not specifically captured by the model and market data are all subject to internal review and approval procedures and consistent application between accounting periods.

18. Share capital

Issued financial instruments, or their components, are classified as equity where they meet the definition of equity and confer on the holder a residual interest in the assets of the Bank.

Incremental costs directly attributable to the issue of an equity instrument are deducted from the initial measurement of the equity instrument.

Accounting Policies

19. Contingent liabilities and assets
A contingent liability is a present obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity or a present obligation that arises from past events but is not recognised because it is not probable that an outflow of resources will be required to settle the obligation or the amount of the obligation cannot be measured with sufficient reliability.

The Bank discloses contingent liabilities and assets in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets.

20. Prospective accounting changes
The following legislative changes and new accounting standards or amendments to standards approved by the International Accounting Standards Board ('IASB') in 2009, (but not already adopted by the Bank) will impact financial reporting in future periods. If applicable they will be adopted in 2010.

The following will be applied in 2010 subject to EU endorsement:

<u>Amendments to IAS 39 Financial Instruments: Recognition and Measurement – Eligible Hedged Items</u>
This clarifies the application of existing principles that determine whether specific risks or portions of cash flows are eligible for designation in a hedging relationship. The amendments will become mandatory for the Bank's 2010 financial statements, with retrospective application required. The amendments are not expected to have a significant impact on the Bank's financial statements.

<u>IFRIC 17 – Distribution of Non-Cash Assets to Owners</u>
This amendment offers guidance on accounting for arrangements whereby an entity distributes non-cash assets to shareholders. This IFRIC is not expected to have a material impact on the Bank.

The following will be applied in 2011 subject to EU endorsement:

<u>Amendment to IAS 24 – Related Party Disclosures</u>
This amendment simplifies the definition of a related party, clarifying its intended meaning and eliminating inconsistencies from the definition. It also provides a partial exemption from the disclosure requirements for government-related entities. This amendment will impact upon the disclosure of related party relationships, transactions and outstanding balances, including commitments in the financial statements of the Bank.

<u>Amendment to IAS 32 – Financial Instruments: Presentation-Classification of rights issues</u>
The amendment states that if rights issues are issued by an entity pro rata to all existing shareholders in the same class for a fixed amount of currency, they should be classified as equity regardless of the currency in which the exercise price is denominated. This amendment is not expected to have a material impact on the Bank's accounts.

<u>IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments</u>
This IFRIC clarifies the requirements of International Financial Reporting Standards (IFRSs) when an entity renegotiates the terms of a financial liability with its creditor and the creditor agrees to accept the entity's shares or other equity instruments to settle the financial liability fully or partially. The impact on the Bank will be dependent on the nature of any future liability management actions, undertaken by the Bank.

Accounting Policies

20. Prospective accounting changes *(continued)*
The following will be applied in 2013 subject to EU endorsement:

IFRS 9 Financial Instruments
IFRS 9 is the first part of the IASB's project to replace IAS 39. The new standard endeavours to enhance the ability of investors and other users of financial information to understand the accounting for financial assets and to reduce complexity. IFRS 9 uses a single approach to determine whether a financial asset is measured at amortised cost or fair value, replacing the many different rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments (its business model) and the contractual cash flow characteristics of the financial assets. The new standard also requires a single impairment method to be used, replacing the many different impairment methods in IAS 39. Thus, IFRS 9 aims to improve comparability and makes financial statements easier to understand for investors and other users.

The first phase of the IAS 39 project as described above has been finalised and awaits EU endorsement. Proposals addressing the second phase, the impairment methodology for financial assets, were published for public comment at the beginning of November 2009.

The implications of Phase 1 as well as the other 2 phases will be examined in due course.

AIB Mortgage Bank

Income statement
for the year ended 31 December 2009

	Notes	**31 Dec 2009 € 000**	31 Dec 2008 € 000
Interest and similar income	1	**892,704**	1,545,921
Interest expense and similar charges	2	**(675,067)**	(1,464,434)
Net interest income		**217,637**	81,487
Trading (loss)	3	**(1,472)**	(11,402)
Other operating income		**4**	18
Other operating expense	4	**(7,106)**	(1,702)
Total operating income		**209,063**	68,401
Administrative expenses	5	**(36,102)**	(39,932)
Operating profit before provisions		**172,961**	28,469
Provisions for impairment of loans and receivables	6	**(78,664)**	(27,182)
Operating profit before taxation		**94,297**	1,287
Taxation on ordinary activities	7	**(11,787)**	(161)
Profit for the year		**82,510**	1,126

The notes on pages 27 to 58 are an integral part of these financial statements.

Chairman Maelíosa ÓhÓgartaigh *Managing Director* David Kelly

Finance Director Michael Keegan *Secretary* David Schorman

25 March 2010

Statement of financial position

as at 31 December 2009

	Notes	**31 Dec 2009 € 000**	31 Dec 2008 € 000
Assets			
Balances at central bank		**50**	25
Loans and receivables to banks	10	**18,208,051**	17,118,044
Loans and receivables to customers	11	**20,692,512**	19,988,151
Other assets	13	**23,328**	35,207
Current taxation		**-**	3,690
Derivative financial instruments	9	**268,351**	241,827
Financial assets held for sale to NAMA	14	**115,008**	-
Assets classified as held for sale	15	**1,184**	-
Total assets		**39,308,484**	37,386,944
Liabilities			
Deposits by banks	16	**27,474,129**	23,182,654
Customer accounts		**175**	234
Derivative financial instruments	9	**3,585**	1,709
Debt securities in issue	17	**10,760,078**	13,168,958
Current taxation		**11,787**	-
Other liabilities		**238**	221
Accruals and deferred income	18	**138,942**	196,128
Subordinated liabilities	19	**300,000**	300,000
Total liabilities		**38,688,934**	36,849,904
Shareholders' equity			
Share capital	20	**450,000**	450,000
Profit and loss account		**169,550**	87,040
Total shareholders' equity		**619,550**	537,040
Total liabilities and shareholders' equity		**39,308,484**	37,386,944

Chairman Maelíosa ÓhÓgartaigh *Managing Director* David Kelly

Finance Director Michael Keegan *Secretary* David Schorman

25 March 2010

Statement of cash flows
for the year ended 31 December 2009

	Notes	**31 Dec 2009 € 000**	31 Dec 2008 € 000
Reconciliation of profit before taxation to net cash inflow from operation activities			
Profit before taxation		**94,297**	1,287
Decrease in prepayments and accrued income		**11,768**	10,331
Decrease in accruals and deferred income		**(57,186)**	(9,049)
(Decrease) /increase in customer accounts		**(59)**	51
Increase in loans and receivables to customers		**(704,361)**	(1,572,001)
Increase in assets held for sale		**(116,192)**	-
(Decrease) /increase in debt securities in issue		**(2,408,880)**	6,085,643
Decrease in derivative financial instruments		**(24,648)**	(324,241)
Increase in loans and receivables to Allied Irish Banks, p.l.c.		**(973,620)**	(8,012,732)
Increase in loans and receivables from Allied Irish Banks, p.l.c.		**4,291,475**	4,351,002
Decrease/ (increase) in other assets		**111**	(340)
Increase/ (decrease) in other liabilities		**17**	(132)
Increase in balances at central bank		**(25)**	-
Net cash inflow from operating assets and liabilities		**112,697**	529,819
Net cash inflow from operating activities before taxation		**112,697**	529,819
Taxation paid		-	(7,407)
Taxation refund		**3,690**	-
Net cash inflow from operating activities		**116,387**	522,412
Financing activities			
Issue of ordinary shares		-	25,000
Dividend Paid		-	(70,000)
Increase in cash and cash equivalents		**116,387**	477,412
Opening cash and cash equivalents		**723,751**	246,339
Closing cash and cash equivalents	24	**840,138**	723,751

AIB Mortgage Bank

Statement of comprehensive income
for the year ended 31 December 2009

	31 Dec 2009 € 000	31 Dec 2008 € 000
Profit for the year	**82,510**	1,126
Other comprehensive income	-	-
Total comprehensive income for the year	**82,510**	1,126

Statement of changes in equity

for the year ended 31 December 2009

	Share capital € 000	Profit and loss account € 000	Total € 000
Balance at 1 January 2008	425,000	155,914	580,914
Dividend paid to parent company	-	(70,000)	(70,000)
Profit attributable to equity holders	-	1,126	1,126
Ordinary shares issued	25,000	-	25,000
Balance at 31 December 2008	450,000	87,040	537,040
Balance at 1 January 2009	**450,000**	**87,040**	**537,040**
Profit attributable to equity holders	-	**82,510**	**82,510**
Balance at 31 December 2009	**450,000**	**169,550**	**619,550**

Notes to the accounts

1. Interest and similar income	**2009 € 000**	2008 € 000
Interest on loans and receivables to customers	**528,467**	935,381
Interest receivable from Allied Irish Banks, p.l.c.	**364,237**	610,540
	892,704	1,545,921

All income earned derives from activities carried out in the Republic of Ireland.

2. Interest expense and similar charges	**2009 € 000**	2008 € 000
Interest payable to Allied Irish Banks, p.l.c.	**341,313**	990,581
Interest on debt securities in issue	**301,683**	448,720
Interest on amounts due to the Central Bank and Financial Services Authority of Ireland	**32,071**	25,133
	675,067	1,464,434

3. Trading (loss)	**2009 € 000**	2008 € 000
Trading (loss)	**(1,472)**	(11,402)

Changes in fair value of interest rate swaps, and certain related account items being hedged, resulted in a trading loss of €1.5m (2008: €11.4m loss). A loss of €1.9m (2008: €8.1m loss) arose as a result of changes in fair value of swaps used to hedge the interest rate risk in the mortgage loan portfolio. While these swaps are highly effective in managing interest rate risk from an economic standpoint, it is not possible to establish accounting fair value hedging relationships between the swaps and the mortgage loan portfolio. As a result the mortgage loan portfolio is not reported at fair value but is reported on an amortised cost basis. This treatment may give rise to volatility in reported income. The balancing gain of €0.4m (2008: €3.3m loss), is in respect of the ineffectiveness of the hedge for mortgage covered securities and represents the difference in the changes to fair value of interest rate swaps and of the related mortgage covered securities being hedged.

Notes to the accounts

4. Other operating expense	2009 € 000	2008 € 000
Fee payable under Government guarantee scheme	**7,106**	1,702

See Note 30 on page 54 for details of AIB Mortgage Bank's relationship (via its parent Allied Irish Banks p.l.c.) with the Irish Government.

5. Administrative expenses	2009 € 000	2008 € 000
Personnel expenses		
Wages and salaries	**361**	409
Social security costs	**39**	48
Retirement benefits	**65**	53
Other personnel expenses	**15**	10
	480	520
Other administrative expenses	**2,409**	2,568
Amounts payable to Allied Irish Banks, p.l.c. under the Outsourcing and Agency Agreement	**33,213**	36,844
	36,102	39,932

6. Provisions for impairment of loans and receivables

	2009			2008		
	Specific **€ 000**	**IBNR** **€ 000**	**Total** **€ 000**	Specific € 000	IBNR € 000	Total € 000
Balance at start of year	**22,146**	**18,397**	**40,543**	7,924	5,437	13,361
Charge against income statement	**48,304**	**30,360**	**78,664**	14,222	12,960	27,182
Transfer to assets held for sale to NAMA	**(2,352)**	**(250)**	**(2,602)**	-	-	-
Transfer to assets classified as held for sale	**(395)**	**-**	**(395)**	-	-	-
At end of year	**67,703**	**48,507**	**116,210**	22,146	18,397	40,543

Notes to the accounts

6. Provisions for impairment of loans and receivables *(continued)*	**2009 € 000**	2008 € 000
By geographic location and industry sector		
Republic of Ireland		
Home mortgages	**116,210**	40,543
	116,210	40,543

7. Taxation	**2009 € 000**	2008 € 000
Current tax		
Profit before tax €94.3m @ 12.5%	**11,787**	161
Total income tax expense	**11,787**	161

The tax charge for the year is at an effective rate of 12.5%, which is the same as the standard Irish corporation tax rate.

8. Risk management

Set out below are details on the risk management framework and interest rate sensitivities for AIB Mortgage Bank.

Risk Management – frameworks

Risk taking is inherent in the provision of financial services and AIB Mortgage Bank, as part of the AIB Group, assumes a variety of risks in undertaking its business activities. Risk is defined as any event that could: damage the core earnings capacity of the Bank, increase earnings or cash flow volatility; reduce capital; threaten business reputation or viability; and/or breach regulatory or legal obligations. AIB Group has adopted an Enterprise Risk Management approach to identifying, assessing and managing risks. The key elements of the framework are:

- Risk philosophy;
- Risk appetite;
- Risk governance and risk management organisation;
- Risk identification and assessment process;
- Risk strategy; and
- Stress and scenario testing.

Notes to the accounts

8. Risk management *(continued)*

Risk Management – Individual risk types

This section provides details of the exposure to, and risk management of, the following individual risk types which have been identified through the AIB Group risk assessment process and which are relevant to AIB Mortgage Bank:-

2.1 Credit risk
2.2 Liquidity risk
2.3 Operational risk
2.4 Regulatory compliance risk
2.5 Non-trading interest rate risk

The 5 applicable risk types are discussed below.

2.1 Credit risk
Credit risk is defined as the risk that a customer or counterparty will be unable or unwilling to meet a commitment that it has entered into and that pledged collateral does not fully cover the Bank's claims. The most significant credit risks assumed by the Bank arise from mortgage lending activities to customers in Ireland. Credit risk also arises in respect of funds placed with AIB in respect of derivatives relating to interest rate risk management.

The Chief Credit Officer of Allied Irish Banks p.l.c. including AIB Mortgage Bank, has overall responsibility for the ongoing credit management of residential home mortgages. It is AIB Group policy to maintain sanctioning authority for residential mortgages independent of the sales function. A credit risk policy has been approved by the Board of Directors of the Bank, is subject to annual review and complies with AIB Group standards. Sophisticated grading tools are used in the management of credit risk and a comprehensive arrears management process ensures that the level of non-performing loans is minimised.

Net disposable income is the key factor in assessing repayment capacity. Repayment capacity is assessed by reference to the debt service ratio which measures the proportion of 'after tax' income required to service the proposed borrowing. When sanctioning mortgage credits, importance is also placed on the loan to value ratios, adequacy of security and the track record of the borrower.

The assessment of individual mortgage loans includes an interest rate stress test in compliance with requirements set by the Central Bank and Financial Services Authority of Ireland.

The ratings influence the management of individual loans. Special attention is paid to lower quality rated loans and, when appropriate, loans are transferred to special units to help avoid default or, when in default, to minimise loss.

The table below sets out the maximum exposure to credit risk that arises within the Bank. The table distinguishes between those assets that are carried in the Statement of Financial Position at amortised cost and those carried at fair value. The most significant credit risks arise from lending activities to customers and banks, derivatives relating to interest rate risk management and 'off-balance sheet' commitments. The credit risks arising from balances at Central Bank are deemed to be negligible based on their maturity and counterparty status.

Notes to the accounts

8. Risk management *(continued)*

Maximum exposure to credit risk

	2009			2008		
	Amortised cost	**Fair value**	**Total**	Amortised cost	Fair value	Total
	€ 000	**€ 000**	**€ 000**	€ 000	€ 000	€ 000
Balances at central banks	**50**	-	**50**	25	-	25
Derivative financial instruments	-	**268,351**	**268,351**	-	241,827	241,827
Loans and receivables to banks	**18,208,051**	-	**18,208,051**	17,118,044	-	17,118,044
Loans and receivables to customers	**20,692,512**	-	**20,692,512**	19,988,151	-	19,988,151
Assets classified as held for sale	**1,184**	**-**	**1,184**	**-**	**-**	**-**
Financial assets held for sale to NAMA	**115,008**	-	**115,008**	**-**	**-**	**-**
Included elsewhere:						
Accrued interest	**23,327**	-	**23,327**	35,207	-	35,207
	39,040,132	**268,351**	**39,308,483**	37,141,427	241,827	37,383,254
Loan commitments	**443,000**	**-**	**443,000**	679,000	-	679,000
Maximum exposure to credit risk	**39,483,132**	**268,351**	**39,751,483**	37,820,427	241,827	38,062,254

Risk identification and assessment

All mortgage loans are subject to an individual underwriting process. In addition, credit risk is identified, assessed and measured through the use of credit rating and scoring tools for each borrower or transaction. The methodology used produces a quantitative estimate of the Probability of Default (PD) for the borrower. This assessment is carried out at the level of the individual borrower or transaction and at portfolio level when relevant.

In the mortgage portfolio, which is characterised by a large number of customers with small individual exposures, risk assessment is largely informed through statistically-based scoring techniques. Both application scoring for new customers and behavioural scoring for existing customers are used to assess and measure risk as well as to facilitate the management of the portfolio.

Role of stress and scenario analysis in the assessment of credit risk

AIB Group conducts periodic stress tests on the mortgage loan portfolio to assess the impact on existing credit concentrations and to assist in the identification of any additional concentrations in its loan books. These tests are carried out as required by senior management.

As outlined above, AIB Mortgage Bank as part of the AIB Group has also instituted stress tests on its credit exposures to assist capital planning under Basel II. The principal elements are as follows:

- Pillar 1 stress test is a scenario analysis of an extreme recession on the portfolio subject to Internal Based Rating systems within the AIB Group. Following the application of the stressed economic scenario to the Bank's grade profiles, the test assesses the incremental impact of the resulting ratings downgrades on the Bank's risk weighted assets and estimates of expected loss and hence capital;
- Pillar 2 stress test is also carried out which applies a more plausible economic stress scenario to the Bank's five year business and financial plans. The credit implications, including concentration risk, are again assessed through modelling the impact of movements in grades across various credit portfolios. The results are combined with the other risk and financial elements to inform capital planning.

Notes to the accounts

8. Risk management *(continued)*

Credit risk *(continued)*

Risk management and mitigation

AIB Mortgage Bank through AIB Group has an established credit process with a framework of a credit policy and delegated authorities, based on skill and experience, for the management and control of credit risk. Credit grading, scoring and monitoring systems accommodate the early identification and management of any deterioration in loan quality. The credit management system is underpinned by an independent system of credit review.

Management approves the credit policy within the parameters of relevant AIB Group level policies. The risk management function is an integral part of the approval process of the Bank's policies. Material Bank policies are referred to the Group Risk Management Committee (RMC) and/or to the Board, where relevant, for approval.

In addition, the Board of AIB Mortgage Bank reviews and approves the credit policy for residential property mortgage loans.

Credit risk mitigation

The most significant and widely used credit risk mitigation tool available to the Bank is its own robust internal credit risk control framework.

Provisioning for impairment

The identification of loans for assessment as impaired is driven by the AIB Group's rating systems. The Group provides for impairment in a prompt and consistent way. The rating models provide a systematic discipline in the identification of loans as impaired and in triggering a need for provisioning on a timely basis.

Loans are identified as impaired if they are past due for typically ninety one days or more or exhibit, through lender assessment, an inability to meet their obligations.

Within its provisioning methodology, the Group uses two types of provisions: a) specific; and b) incurred but not reported ("IBNR") – i.e. collective provisions for earning loans.

Specific provisions

A specific provision is made against problem loans when, in the judgement of management, the estimated repayment realisable from the obligor, including the value of any security available, is likely to fall short of the amount of principal and interest outstanding on the obligor's loan account. The amount of the specific provision made in AIB Mortgage Bank's financial statements is intended to cover the difference between the balance outstanding on impaired loans and estimated recoveries (i.e. the present value of future cash flows). When raising specific provisions, AIB Mortgage Bank divides its impaired portfolio into two categories namely, Individually significant and Individually insignificant.

Notes to the accounts

8. Risk management *(continued)*

Credit risk *(continued)*
Individually significant impairment
Each entity of AIB Group sets a threshold above which cases are assessed on an individual basis. For those credits identified as being impaired, the individual impairment provision is calculated by discounting the expected future cash flows at the exposure's effective interest rate and comparing the result (the estimated recoverable amount) to the carrying amount of the loan to determine the level of provision required. The key inputs to the discounted cash flow models are the estimated amount and timing of cash flows (to include scheduled repayments, interest payments or payments due from realisation of security) and the exposure's effective interest rate.

Individually insignificant impairment
The calculation of an impairment charge for credits below the "significant" threshold is undertaken on a collective basis. Loans are grouped together in homogeneous pools sharing common characteristics and impairment is calculated by reference to the loss history experience for the asset pool (i.e. amount and timing of cash flows / loss given default).

When a loan has been subjected to a specific provision and the prospects for recovery do not improve, a point will come when it may be concluded that there is no realistic prospect of recovery. When that point is reached, the amount of the loan which is considered to be beyond prospect of recovery is charged off.

The management process for the identification of loans requiring provision is underpinned by independent tiers of review. Credit quality and loan loss provisioning are independently monitored on a regular basis. A Group wide system for rating advances according to agreed credit criteria exists with an important objective being the timely identification of vulnerable loans so that remedial action can be taken at the earliest opportunity. The rating of an exposure is fundamental to the determination of provisioning in AIB Mortgage Bank; it triggers the process which results in the creation of a specific provision on individual loans where there is doubt on recoverability.

Collective impairment for performing book (Incurred but not reported loss)
IBNR provisions are maintained to cover loans which are impaired at the Statement of Financial Position date and, while not specifically identified, are known from experience to be present in any portfolio of loans. IBNR provisions can only be recognised for incurred losses and are not permitted for losses that are expected to happen as a result of likely future events. IBNR provisions are determined by reference to loss experience in the portfolios and to the credit environment at the Statement of Financial Position date.

IBNR provisions are maintained at levels that are deemed appropriate by management having considered: credit grading profiles and grading movements; historic loan loss rates; changes in credit management procedures, processes and policies; levels of credit management skills; local and international economic climates; and portfolio profile / industry conditions.

The approach used for the collective evaluation of impairment is to split the performing financial assets into homogeneous pools on the basis of similar risk characteristics. The asset pools are multiplied by the "average annual loss rate" for that pool, suitably adjusted where appropriate for any factors currently affecting the portfolio that may not have been a feature in the past or vice versa. The resultant amount is then adjusted to reflect the Emergence Period, i.e. the time it takes following a loss event for an individual loan to be recognised as impaired requiring a specific provision.

The Emergence Period is key in determining the level of collective provisions. The Emergence Period is determined by taking into account current credit management practices, historical evidence of assets moving from "good" to "bad" as a result of a "loss event" and will include actual case studies. The Emergence Period applied in AIB Mortgage Bank is 6 months.

The level of IBNR provisions is reviewed quarterly to ensure it remains appropriate and adequate.

Notes to the accounts

8. Risk management *(continued)*

Credit risk *(continued)*
Risk monitoring and reporting
Relevant credit risk information is reported in a timely manner to the appropriate level to enable informed management decision making.

Credit managers receive sufficient account and customer information to pro-actively manage the Bank's credit risk exposures at a transaction and relationship level.

Further information on credit risk
Further information on credit risk can be found in the notes to the financial statements.
- Derivative financial instruments *(note 9).*
- Loans and receivables to banks *(note 10).*
- Loans and receivables to customers *(note 11).*
- Provisions for impairment of loans and receivables *(note 6).*
- Financial assets held for sale to NAMA *(note 14).*

2.2 Liquidity risk
Liquidity risk is the exposure to loss from not having sufficient funds available at an economic price to meet actual and contingent commitments. The objective of liquidity management is to ensure that, at all times, the Bank holds sufficient funds to meet its contracted and contingent commitments and regulatory requirements, at an economic price.

AIB Mortgage Bank's liquidity risk is managed as part of the overall AIB Group liquidity management. This includes the risk identification and assessment, risk management and mitigation, and risk monitoring and reporting processes.

Funding and Liquidity
The funding and liquidity policy as approved by the Board of Directors of the Bank sets out the forms of funding which can be used by the Bank to meet its liquidity requirements – see below. It also sets out the outsourcing arrangements which have been established with Allied Irish Banks p.l.c. to source and manage the funding and liquidity requirements. The policy also specifies reporting requirements with respect to funding and liquidity management.

Funding
The Bank is authorised to fund the assets it holds through the following forms of funding:

(a) the issuance of Mortgage Covered Securities in accordance with the ACS Acts;

(b) borrowing funds from Allied Irish Banks p.l.c.;

(c) borrowing from the CBFSAI under a Mortgage-Backed Promissory Note (short term) facility ("MBPN Facility");

(d) wholesale and corporate market deposit taking; and

(e) capital funding to ensure at a minimum compliance with the capital adequacy requirements of the Financial Regulator.

Notes to the accounts

8. Risk management *(continued)*

Funding and Liquidity *(continued)*
The MPBN Facility is secured by a floating charge over a pool of the Bank's home loans and related security which is separate to the Pool (that secures the Mortgage Covered Securities) maintained by the Issuer in accordance with the ACS Acts

Liquidity
Liquidity requirements for EU credit institutions are not the subject matter of EU directives. The Financial Regulator requires credit institutions to comply with a cashflow maturity mismatch approach for the management of their liquidity. This involves credit institutions analysing their cash flows on a group-wide basis under various headings and placing them in pre-determined time bands depending on when the cash is received or paid out. Limits are imposed on the group on the first (0-8 days) and the second (8-31 days) time bands and monitoring ratios will be calculated for subsequent time bands. These requirements apply to AIB on a consolidated basis rather than to the Bank on a solo basis. The Bank complies with its liquidity reporting obligations as part of the AIB Group consolidated reporting permitted by the Financial Regulator.

The primary liquidity requirements of the Bank are to have sufficient funds available at an economic price to meet its commitments to pay interest and principal to holders of the Issuer's Mortgage Covered Securities, to repay short term borrowings under the MBPN Facility and to lend to mortgage customers in accordance with outstanding offer letters.

The Bank's liquidity risk is managed as part of the overall AIB Group liquidity management.

AIB Global Treasury (part of the AIB Capital Markets division) through the Outsourcing and Agency Agreement:

- supports the liquidity management requirements of the Bank taking into account the regulatory framework at a Group level;

- ensures that the Bank's liquidity management complies with AIB Group liquidity policy.

It is the Bank's policy to ensure that resources are at all times available to meet the Bank's obligations. The Bank meets its day to day residual funding requirements through borrowing facilities in place with Allied Irish Banks, p.l.c.. The table on page 38 analyses the liabilities into relevant maturity groupings based on the remaining period at the reporting date to contractual maturity date.

2.3 Operational risk
Operational risk, which is inherent in all business activities, is the exposure to loss from inadequate or failed internal processes, people and systems, or from external events.

The management of operational risk is a line management responsibility. It is supported by specialist operational risk management ('ORM') functions within Allied Irish Banks, p.l.c. that assist and advise line management on specific operational risks. Examples include money laundering prevention, compliance, business continuity planning, information security and insurance.

An element of AIB Mortgage Bank's ORM programme is an operational risk self-assessment process. This process requires the Bank to assess its operational risks and the effectiveness of the related controls to address these risks. It complements the risk-based audit approach applied by internal audit in its role as independent assessor of management's control and risk management processes.

Notes to the accounts

8. Risk management *(continued)*

2.4 Regulatory compliance risk
Regulatory compliance risk is defined as the risk of regulatory sanctions, material financial loss or loss to reputation which the Bank may suffer as a result of failure to comply with all applicable laws, regulations, rules, related self regulatory standards and codes of conduct applicable to its activities.

AIB Mortgage Bank's regulatory compliance risk is managed as part of the overall AIB Group Regulatory compliance framework. This includes risk identification and assessment, risk management and mitigation, and risk monitoring and reporting processes.

2.5 Non-trading interest rate risk
Interest rate risk is the exposure of the Bank's earnings to movements in market interest rates. The Bank is exposed to risk of interest rate fluctuations to the extent that assets and liabilities mature or reprice at different times or in differing amounts.

The Bank is exposed to interest-rate risk arising from mortgage lending activities and the issuance of Mortgage Covered Securities. Interest rate swaps, as explained in the paragraphs below, are used to manage this exposure.

Interest-rate risk arising from the issuance of fixed-rate Mortgage Covered Securities is managed through interest rate swaps with AIB which have the effect of transforming fixed-rate liability risk into floating-rate risk.

The interest rate exposure of the Bank relating to its Irish residential lending is managed using two macro interest rate swaps with Allied Irish Banks, p.l.c. one of which, the Pool Hedge, relates only to the Pool and Mortgage Covered Securities issued by the Bank and the other of which (the Non-Pool Hedge) relates only to Irish residential loans which are not included in the Pool. This split is required by the Asset Covered Securities Acts.

The Pool Hedge and the Non Pool Hedge contracts entail the monthly payment of the average customer rate on these mortgages and in return, the receipt of 1 month Euribor plus the current margin being achieved on the mortgage portfolio. The contract is reset each month to reflect the outstanding mortgage balances at that time and to reflect updated customer rates, Euribor and margin levels. Settlements are made between the Bank and Allied Irish Banks p.l.c. to reflect the net amount payable/receivable in each month.

After taking account of the effect of interest rate swaps, the Bank's remaining interest rate exposure arises mainly from variable interest rate mortgage loans, where the interest rate for the majority of the loans is based on the ECB Refinancing Rate, whereas the related funding cost is based on Euribor rates.

Notes to the accounts

8. Risk management *(continued)*

Non-trading interest rate risk *(continued)*

Interest rate swaps are used solely for risk management and not trading purposes.

The nominal values of the swaps are set out in note 9.

The Bank is not exposed to any other market risks, i.e. foreign exchange rates or equity prices.

Further details of AIB Group’s Liquidity Risk, Operational Risk, Regulatory Compliance Risk and Non-Trading Interest Rate Risk frameworks are set out in the Annual Report of Allied Irish Banks, p.l.c.

Interest rate sensitivity

The net interest rate sensitivity of AIB Mortgage Bank at 31 December 2009 is illustrated in the following table. This information is presented for eight different time periods reflecting the balances of assets and liabilities with rates that are subject to change within each period, data regarding balances which are not sensitive to interest rate movements and any rate sensitive off-balance sheet contracts. The table shows the sensitivity of the Statement of Financial Position at one point in time and is not necessarily indicative of positions at other dates. In developing the classifications used in the table it has been necessary to make certain assumptions and approximations in assigning assets and liabilities to different repricing categories.

AIB Mortgage Bank

Interest Rate Sensitivity
Interest Rate Sensitivity analysis for the Bank at **31 December 2009** is as follows:

Assets	**0 ≤ 1 mth**	**1 ≤ 3 mths**	**3 ≤ 12 mths**	**1 ≤ 2yrs**	**2 ≤ 3yrs**	**3 ≤ 4yrs**	**4 ≤ 5yrs**	**5yrs+**	**Rate Insensitive**	**Total**
	€ 000	**€ 000**	**€ 000**	**€ 000**	**€ 000**	**€ 000**	**€ 000**	**€ 000**	**€ 000**	**€ 000**
Cash and balances at central bank	50	-	-	-	-	-	-	-	-	50
Loans and receivables to customers	18,835,739	88,300	656,597	563,111	309,139	59,709	107,349	72,568	-	20,692,512
Loans and receivables to banks	18,208,051	-	-	-	-	-	-	-	-	18,208,051
Derivatives and other financial instruments	-	-	-	-	-	-	-	-	268,351	268,351
Assets classified as held for sale	1,184	-	-	-	-	-	-	-	-	1,184
Financial assets held for sale to NAMA	115,008	-	-	-	-	-	-	-	-	115,008
Other assets	-	-	-	-	-	-	-	-	23,328	23,328
Total assets	**37,160,032**	**88,300**	**656,597**	**563,111**	**309,139**	**59,709**	**107,349**	**72,568**	**291,679**	**39,308,484**
Liabilities										
Customer accounts	-	-	-	-	-	-	-	-	175	175
Deposits by banks	27,474,129	-	-	-	-	-	-	-	-	27,474,129
Derivatives and other financial instruments	-	-	-	-	-	-	-	-	3,585	3,585
Debt issued	7,750,000	-	-	-	-	1,000,000	-	1,740,000	270,078	10,760,078
Subordinated liabilities	300,000	-	-	-	-	-	-	-	-	300,000
Other liabilities	-	-	-	-	-	-	-	-	150,967	150,967
Shareholders’ funds	-	-	-	-	-	-	-	-	619,550	619,550
Total liabilities	**35,524,129**	**-**	**-**	**-**	**-**	**1,000,000**	**-**	**1,740,000**	**1,044,355**	**39,308,484**
Derivative financial instruments (Interest rate swaps)										
Floating rate interest receivable	20,933,425	-	-	-	-	-	-	-	-	20,933,425
Floating rate interest payable	(19,076,652)	(88,300)	(656,597)	(563,111)	(309,139)	(59,709)	(107,349)	(72,568)	-	(20,933,425)
Floating rate interest payable	(4,740,000)	-	-	-	-	-	-	-	-	(4,740,000)
Fixed rate interest receivable	2,000,000	-	-	-	-	1,000,000	-	1,740,000	-	4,740,000
Total derivatives	**(883,227)**	**(88,300)**	**(656,597)**	**(563,111)**	**(309,139)**	**940,291**	**(107,349)**	**1,667,432**	**-**	**-**
Interest sensitivity gap	752,676	-	-	-	-	-	-	-	(752,676)	-
Cumulative interest sensitivity gap	752,676	752,676	752,676	752,676	752,676	752,676	752,676	752,676	-	-

AIB Mortgage Bank

Interest Rate Sensitivity
Interest Rate Sensitivity analysis for the Bank at **31 December 2008** is as follows:

Assets	**0 ≤ 1 mth**	**1 ≤ 3 mths**	**3 ≤ 12 mths**	**1 ≤ 2yrs**	**2 ≤ 3yrs**	**3 ≤ 4yrs**	**4 ≤ 5yrs**	**5yrs+**	**Rate Insensitive**	**Total**
	€ 000	**€ 000**	**€ 000**	**€ 000**	**€ 000**	**€ 000**	**€ 000**	**€ 000**	**€ 000**	**€ 000**
Cash and balances at central bank	25	-	-	-	-	-	-	-	-	25
Loans and receivables to customers	18,615,659	84,536	306,856	406,545	353,259	105,584	42,625	73,087	-	19,988,151
Loans and receivables to banks	17,118,044	-	-	-	-	-	-	-	-	17,118,044
Derivatives and other financial instruments	-	-	-	-	-	-	-	-	241,827	241,827
Assets classified as held for sale	-	-	-	-	-	-	-	-	-	-
Financial assets held for sale to NAMA	-	-	-	-	-	-	-	-	-	-
Other assets	-	-	-	-	-	-	-	-	38,897	38,897
Total assets	**35,733,728**	**84,536**	**306,856**	**406,545**	**353,259**	**105,584**	**42,625**	**73,087**	**280,724**	**37,386,944**
Liabilities										
Customer accounts	-	-	-	-	-	-	-	-	234	234
Deposits by banks	23,182,654	-	-	-	-	-	-	-	-	23,182,654
Derivatives and other financial instruments	-	-	-	-	-	-	-	-	1,709	1,709
Debt issued	5,750,000	-	2,500,000	2,000,000	-	-	1,000,000	1,675,000	243,958	13,168,958
Subordinated liabilities	300,000	-	-	-	-	-	-	-	-	300,000
Other liabilities	-	-	-	-	-	-	-	-	196,349	196,349
Shareholders' funds	-	-	-	-	-	-	-	-	537,040	537,040
Total liabilities	**29,232,654**	**-**	**2,500,000**	**2,000,000**	**-**	**-**	**1,000,000**	**1,675,000**	**979,290**	**37,386,944**
Derivative financial instruments										
(Interest rate swaps)										
Floating rate interest receivable	20,024,875	-	-	-	-	-	-	-	-	20,024,875
Floating rate interest payable	(18,652,383)	(84,536)	(306,856)	(406,545)	(353,259)	(105,584)	(42,625)	(73,087)	-	(20,024,875)
Floating rate interest payable	(7,175,000)	-	-	-	-	-	-	-	-	(7,175,000)
Fixed rate interest receivable	-	-	2,500,000	2,000,000	-	-	1,000,000	1,675,000	-	7,175,000
Total derivatives	**(5,802,508)**	**(84,536)**	**2,193,144**	**1,593,455**	**(353,259)**	**(105,584)**	**(957,375)**	**1,601,913**	-	-
Interest sensitivity gap	698,566	-	-	-	-	-	-	-	(698,566)	
Cumulative interest sensitivity gap	698,566	698,566	698,566	698,566	698,566	698,566	698,566	698,566	-	

Notes to the accounts

9. Derivatives and other financial instruments

Set out below are details on fair values and derivative information for AIB Mortgage Bank.

The Bank uses two different types of interest rate swaps to hedge interest rate risk. The first type is used to hedge interest rate risk on mortgage loan accounts both within the Cover Assets Pool and outside the Cover Assets Pool, effectively converting interest receivable from a fixed rate basis to a floating rate basis. Although these swaps are considered to be an effective hedge in economic terms, due to their nature, it has not been possible to establish a "fair value" hedging relationship under IAS 39 with the mortgage loan accounts and consequently, they are classified as "Trading".

The second type of interest rate swaps are vanilla interest rate swaps used to hedge the mortgage covered securities, converting interest payable from a fixed rate basis to a floating rate basis. Effective fair value hedging relationships (as stipulated by IAS 39) have been established between these swaps and the underlying covered bonds and consequently the change in fair value of the swaps is largely offset by fair value movements in the covered bonds themselves.

All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative. Allied Irish Banks, p.l.c. is the counterparty to all derivative contracts noted below.

	2009 € 000 Contract/ Notional Amount	**2009 € 000 Fair Value Asset/ (Liability)**	2008 € 000 Contract/ Notional Amount	2008 € 000 Fair Value Asset/ (Liability)
Derivatives classified as trading				
Hedging mortgage loan accounts – outside the Cover Assets Pool	**4,859,809**	**(503)**	5,942,574	(269)
Hedging mortgage loan accounts – within the Cover Assets Pool	**16,073,616**	**(3,082)**	14,082,301	(1,440)
Total derivatives classified as trading	**20,933,425**	**(3,585)**	20,024,875	(1,709)
Derivatives classified as hedging (Debt Securities)				
Interest rate swaps	**4,740,000**	**268,351**	7,175,000	241,827
Total derivatives classified as hedging (Debt Securities)	**4,740,000**	**268,351**	7,175,000	241,827
Total derivatives	**25,673,425**	**264,766**	27,199,875	240,118

The following table represents the underlying principal and gross replacement costs of the Bank's derivatives as at 31 December 2009.

	Residual Maturity 2009				Residual Maturity 2008			
31 December 2009	**Within one year € 000**	**1 to 5yrs € 000**	**Over 5yrs € 000**	**Total € 000**	Within one year € 000	1 to 5yrs € 000	Over 5yrs € 000	Total € 000
Underlying principal amount								
Interest rate contracts	**22,933,425**	**1,000,000**	**1,740,000**	**25,673,425**	22,524,875	3,000,000	1,675,000	27,199,875
Gross replacement costs								
Interest rate contracts	**74,239**	**79,813**	**251,320**	**405,372**	68,253	160,241	208,453	436,947

Notes to the accounts

9. Derivatives and other financial instruments *(continued)*

These tables present the notional and fair value amounts; weighted average maturity and weighted average receive and pay rates for instruments held for risk management purposes entered into by the Bank in 2009.

	Notional principal amount	Weighted average maturity in years	Weighted average rate Receive	Pay	Estimated Fair Value
	€ 000		%	%	€ 000
Interest rate derivatives designated as fair value hedges					
Receive fixed					
1 year or less					4,993
1-5 years					54,539
Over 5 years					208,819
	4,740,000	**3.52**	**4.17**		**268,351**
Pay floating					
1 year or less					
1-5 years					
Over 5 years					
	4,740,000	**0.08**		**0.54**	
Other Interest rate derivatives*					
Interest rate swaps:					
Pay floating					
1 year or less					
1-5 years					(39,296)
Over 5 years					
	20,933,425	**0.08**		**2.37**	**(39,296)**
Receive floating					
1 year or less					35,711
1-5 years					
Over 5 years					
	20,933,425	**0.08**	**2.15**		**35,711**

* These swaps are used to hedge the mortgage loan portfolio but do not qualify for fair value hedge accounting.

All derivative instruments are deemed to be Level 2 instruments as they have been valued using valuation techniques which use observable market data. There have been no transfers into or out of Level 2 during the year and the valuation techniques applied are consistent with the prior year.

Notes to the accounts

9. Derivatives and other financial instruments *(continued)*

Fair value of financial instruments
The term "financial instruments" includes financial assets, financial liabilities and derivatives. The fair value of a financial instrument is the amount for which an asset could be exchanged or a liability settled, between knowledgeable, willing parties in an arms length transaction.

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

Fair value information is not provided for certain financial instruments or for items that do not meet the definition of a financial instrument. The fair value information presented does not purport to represent, nor should it be construed to represent, the underlying value of the Bank as a going concern at 31 December 2009.

The following table gives details of the carrying amounts and fair values of financial instruments.

	2009 Carrying Amount € 000	**2009 Fair value Amount € 000**	2008 Carrying Amount € 000	2008 Fair Value Amount € 000
Assets				
Cash and balances at central bank	**50**	**50**	25	25
Derivative financial instruments	**268,351**	**268,351**	241,827	241,827
Loans and receivables to banks	**18,208,051**	**18,208,051**	17,118,044	17,118,044
Loans and receivables to customers	**20,692,512**	**20,734,773**	19,988,151	20,015,279
Assets classified as held for sale	**1,184**	**1,184**	-	-
Financial assets held for sale to NAMA	**115,008**	**115,016**	-	-
Liabilities				
Deposits by banks	**27,474,129**	**27,474,129**	23,182,654	23,182,654
Customer accounts	**175**	**175**	234	234
Derivative financial instruments	**3,585**	**3,585**	1,709	1,709
Debt securities in issue	**10,760,078**	**10,760,078**	13,168,958	13,168,958
Subordinated liabilities	**300,000**	**171,000**	300,000	171,580

Notes to the accounts

9. Derivatives and other financial instruments *(continued)*

The following methods and assumptions were used in estimating the fair value of financial instruments.

Loans and receivables to banks, loans and receivables to customers and financial assets held for sale to NAMA
The fair value of loans and receivables to banks and financial assets held for sale to NAMA were estimated using discounted cash flows applying either market rates, where practicable, or rates currently offered by other financial institutions for placings with similar characteristics. The fair value of the financial assets held for sale to NAMA does not take into account the value at which these loans may transfer to NAMA.

The Bank provides lending facilities of varying rates and maturities to personal customers. The carrying amount of variable rate loans was considered to be at market value if there was no significant change in the credit risk of the borrower. The fair value of fixed rate loans was calculated by discounting expected cash flows using discount rates that reflected the credit and interest rate risk in the portfolio.

Deposits by banks, customer accounts and debt securities in issue
The fair value of deposits by banks is equal to their book value. The fair value of debt securities in issue is estimated using discounted cash flows applying either market rates, where applicable, or interest rates currently offered by the Bank.

Subordinated liabilities
The fair value of the subordinated liabilities was estimated using discounted cash flows. In all cases, redemption prior to maturity is subject to the necessary prior approval of the Central Bank and Financial Services Regulatory Authority of Ireland.

Derivative financial instruments
The Bank uses various derivatives, designated as hedges, to manage its exposure to fluctuations in interest rates. The fair value of these instruments is estimated using market prices or pricing models consistent with the methods used in AIB Group for valuing similar instruments used for trading purposes.

Assets classified as held for sale
The fair value of assets held for sale is equal to their book value.

10. Loans and receivables to banks	**2009** **€ 000**	2008 € 000
Funds placed with Allied Irish Banks, p.l.c.		
Analysed by remaining maturity:		
- 3 months or less	**9,718,051**	4,193,044
- 1 year or less but over 3 months	**-**	2,500,000
- 5 years or less but over 1 year	**6,750,000**	8,750,000
- Greater than 5 years	**1,740,000**	1,675,000
	18,208,051	17,118,044

Notes to the accounts

11. Loans and receivables to customers	2009 € 000	2008 € 000
Analysed by remaining maturity:		
- 3 months or less	**288,880**	193,220
- 1 year or less but over 3 months	**634,185**	558,234
- 5 years or less but over 1 year	**3,358,373**	2,961,592
- Greater than 5 years	**16,527,284**	16,315,648
Provisions for impairment of loans and receivables (note 6)	**(116,210)**	(40,543)
	20,692,512	19,988,151

The unwind of the discount on the impairment provision amounted to €1.9m (2008: €230k) and is included in the carrying value of loans and receivables to customers. This has been credited to interest income.

Loans and receivables to customers comprise only the AIB branch originated residential mortgage loan portfolio in the Republic of Ireland. This portfolio is well diversified by borrower, by market segment and by geographical location.

By geographic location and sector	2009 € 000	2008 € 000
Republic of Ireland		
Home mortgages (net of provisions)	**20,692,512**	19,988,151
	20,692,512	19,988,151

12. Additional information on credit risk

Aged analysis of contractually past due but not impaired facilities – 31 December 2009

	1-30days € 000	31-60days € 000	61-90days € 000	91+days € 000	Total € 000
Home mortgages	**238,987**	**102,390**	**58,049**	**78,352**	**477,778**
	238,987	**102,390**	**58,049**	**78,352**	**477,778**

Notes to the accounts

12. Additional information on credit risk *(continued)*

Aged analysis of contractually past due but not impaired facilities – 31 December 2008

	1-30days € 000	31-60days € 000	61-90days € 000	91+days € 000	Total € 000
Home mortgages	126,540	83,150	58,890	16,350	284,930
	126,540	83,150	58,890	16,350	284,930

As at 31 December 2009, there were no mortgage loan accounts (Nil in 2008) in default in the Cover Assets Pool (in default being defined as mortgage loan accounts in arrears by three months or more) - refer to Note 17(c).

Individually impaired loans by geographic location and sector

	2009 € 000	2008 € 000
Republic of Ireland		
Home mortgages	**381,740**	134,500
	381,740	134,500

Collateral and other credit enhancements

The Bank takes collateral in support of its lending activities when deemed appropriate and has a series of policies and procedures in place for the assessment, valuation and taking of such collateral.

The main types of collateral for loans and receivables to customers are as follows:

Retail Mortgages; the Bank takes collateral in support of lending transactions for the purchase of residential property. There are clear policies in place which set out the type of property acceptable as collateral and the relationship of loan to property value. All properties are required to be fully insured and be subject to a legal charge in favour of the Bank.

Notes to the accounts

13. Other assets	2009 € 000	2008 € 000
Accrued interest	**22,645**	34,413
Other assets	**683**	794
	23,328	35,207

14. Financial assets held for sale to NAMA

On 7 April 2009, the Minister for Finance announced the Government's intention to establish a National Asset Management Agency ("NAMA") and on 22 November 2009, the NAMA Act was enacted providing for the establishment of NAMA. The purposes of the NAMA Act include the restoration of stability to the banking system and the facilitation of restructuring of credit institutions of systemic importance to the Irish economy. The Government has acknowledged AIB's systemic importance to the Irish economy in the context of the Credit Institutions (Financial Support) Scheme 2008 and by virtue of the €3.5 billion investment in the Group by the National Pension Reserve Fund Commission Investment ("NPRFC") in 2009. The participation of AIB (including AIB Mortgage Bank) in the NAMA programme was approved by shareholders at an Extraordinary General Meeting held on 23 December 2009. In respect of the actual transfer process, assets to be transferred to NAMA from AIB Mortgage Bank will firstly transfer from AIB Mortgage Bank to Allied Irish Banks, p.l.c. at fair value for onward transfer to NAMA. The fair value attaching to the transferred assets will be based on the valuation NAMA place on the transferred assets.

The table below provides an analysis of the assets that may transfer to NAMA by original Statement of Financial Position classification. These assets have been measured at the lower of carrying amount and fair value less costs to sell in accordance with the accounting policy for such assets.

	2009 € 000	2008 € 000
Loans and receivables held for sale to NAMA *	**114,846**	-
Accrued income on assets held for sale to NAMA	**162**	-
	115,008	**-**

* Net of provisions of €2.6m

Loans and receivables held for sale to NAMA by geographic location and sector

	2009 € 000	2008 € 000
Republic of Ireland		
Home Mortgages (net of provisions)	**115,008**	**-**
	115,008	**-**

Notes to the accounts

14. Financial assets and financial liabilities held for sale to NAMA *(continued)*

Aged analysis of contractually past due but not impaired facilities held for sale to NAMA – 31 December 2009

	1-30days € 000	31-60days € 000	61-90days € 000	91+days € 000	Total € 000
Republic of Ireland					
Home mortgages	**2,960**	**1,490**	**150**	**1,590**	**6,190**
	2,960	**1,490**	**150**	**1,590**	**6,190**

Individually impaired loans held for sale to NAMA by geographic location and sector

	2009 € 000	2008 € 000
Republic of Ireland		
Home mortgages	**10,321**	-
	10,321	-

15. Assets classified as held for sale

At 31 December 2009, the Bank has classified certain assets as held for sale other than those held for sale to NAMA. The assets classified as held for sale reported total of €1.2m comprises solely of repossessed assets.

Repossessed assets relate to defaulted buy to let loans where the Bank has taken possession of the underlying security and consists of residential properties.

16. Deposits by banks	2009 € 000	2008 € 000
Due to Allied Irish Banks, p.l.c.	**25,974,129**	23,182,654
Due to Central Bank*	**1,500,000**	-
	27,474,129	23,182,654

The Bank has a borrowing facility with its parent company, Allied Irish Banks, p.l.c., under which the parent company provides the balance of funding after the Bank has availed of other sources of funds.

*At 31 December 2009, of the €3.5bn mortgaged covered securities issued to AIB Mortgage Bank, €1.5bn was the subject of a sale and repurchase agreement with the ECB with a maturity date of 23 December 2010.

Notes to the accounts

16. Deposits by banks *(continued)*

At 31 December 2009 and 2008 no deposits by Bank's are secured by way of charge to the Central Bank and Financial Services Authority of Ireland ("CBFSAI"). Under the terms of the Mortgage-Backed Promissory Note ('MBPN') programme with the CBFSAI, such obligations are secured by way of a first floating charge to the CBFSAI over all its right, title, interest and benefit in loans and receivables to customers. Otherwise than with the prior written consent of the CBFSAI, the Bank had pledged under the terms of the floating charge to maintain the assets so charged free from any encumbrance and otherwise than in the ordinary course of business not to sell, transfer, lend or otherwise dispose of any part of the charged assets.

17. Debt securities in issue	**2009** **€ 000**	2008 € 000
Mortgage covered securities in issue by remaining maturity:		
- 1 year or less	**2,005,257**	2,509,682
- 5 years or less but over 1 year	**6,804,806**	8,816,428
- Greater than 5 years	**1,950,015**	1,842,848
	10,760,078	13,168,958

Mortgage covered securities in issue to external investors and internal issuances at nominal value:

- External investors	**4,740,000**	7,175,000
- Allied Irish Banks, p.l.c.	**5,750,000**	5,750,000
- AIB Mortgage Bank	**3,500,000**	-
	13,990,000	12,925,000

Mortgage covered securities issued as a self issuance to AIB Mortgage Bank are not recognised in the Statement of Financial Position. As the bearer securities and the mortgage covered securities do not meet the criteria of an asset and a liability under the IASB Framework, no asset or liability has been recognised. The self issuance of securities is however disclosed above. When self issuances of mortgage covered securities are the subject of a sale and repurchase agreement with the ECB, the transaction gives rise to the recognition of an asset and a liability. (See note16).

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

At 31 December 2009, the Cover Assets Pool amounted to €19.6bn (€16.6bn in 2008), comprising of €16.1bn (€14.1bn in 2008) of mortgage credit assets (mortgage loan accounts) and €3.5bn (€2.5bn in 2008) of substitution assets (cash on deposit with Allied Irish Banks, p.l.c.). Section 40 (2) of the Act requires that the following information be disclosed in respect of mortgage credit assets that are recorded in the register of mortgage covered securities business.

Notes to the accounts

17. Debt securities in issue *(continued)*

17 (a) Mortgaged properties and principal loan balances outstanding in the cover assets pool
Total Loan Balances

From	To	Total Loan Balances (1 & 2) 2009 € m	Number of Mortgaged Properties 2009	Total Loan Balances (1 & 2) 2008 € m	Number of Mortgaged Properties 2008
0	€100,000	**1,858**	**36,450**	1,723	34,735
€100,000	€200,000	**4,553**	**31,038**	3,692	25,478
€200,000	€500,000	**7,393**	**25,746**	6,421	22,225
Over €500,000		**2,270**	**2,834**	2,266	2,648
		16,074	**96,068**	14,102	85,086

(1) The total loan balances are categorised by the total loan balance outstanding per mortgaged property, including principal and interest charged to the loan accounts, but excluding interest accrued but not charged to the loan accounts.

(2) There could be one or more loan accounts per mortgaged property. The Cover Assets Pool contains 112,121 loan accounts (98,613 in 2008) secured on 96,068 properties (85,086 in 2008).

17 (b) Geographical location of mortgaged properties in the cover assets pool

Geographical Area	Number of Mortgaged Properties 2009		Number of Mortgaged Properties 2008	
Co. Dublin	**20,454**	**21%**	17,583	21%
Outside Dublin	**75,614**	**79%**	67,503	79%
	96,068	**100%**	85,086	100%

17 (c) Mortgage loan accounts in default in the cover assets pool

As at 31 December 2009, there were no mortgage loan accounts (Nil in 2008) in default in the Cover Assets Pool (in default being defined as mortgage loan accounts in arrears by three months or more).

17 (d) Mortgage loan accounts in default in the cover assets pool with arrears greater than €1,000

During the year ended 31 December 2009, 180 mortgage loan accounts (400 in 2008) in the Cover Assets Pool had been in default with arrears greater than €1,000. As at 31 December 2009, there were no accounts in default in the Cover Assets Pool (Nil in 2008).

17 (e) Replacement of non-performing mortgage loan accounts from the cover assets pool

During the year ended 31 December 2009, 1,241 non-performing mortgage loan accounts (1,289 in 2008) were removed in total from the Cover Assets Pool. (For this purpose, non-performing is defined as in arrears by three months or more, i.e. has the same meaning as in default.) These loan accounts were not replaced with other assets as the Cover Assets Pool continued to meet all regulatory requirements.

Notes to the accounts

17. Debt securities in issue *(continued)*

17 (f) Amount of interest in arrears on mortgage loan accounts in the cover assets pool not written off

The total amount in arrears (including principal and interest) in respect of the 503 accounts (647 in 2008) as at 31 December 2009 was €614,259 (€817,982 in 2008). None of the accounts in question were written off as at 31 December 2009, as they were in arrears by less than three months.

17 (g) Total principal and interest payments on mortgage loan accounts

The total amount of repayments (principal and interest) made by customers on mortgage loan accounts in the Cover Assets Pool during the year ended 31 December 2009 was €1,393m (€2,005m in 2008), of which €998m (€1,350m in 2008) represented repayment of principal and €395m (€655m in 2008) represented payment of interest. The repayments of principal include the repayment of mortgage loan accounts by customers closing their existing accounts when opening a new account.

17 (h) Number and amount of mortgage loans in the cover assets pool secured on commercial property

As at 31 December 2009 there were no loan accounts (Nil in 2008) in the Cover Assets Pool that were secured on commercial properties.

18. Accruals and deferred income	**2009** **€ 000**	2008 € 000
Interest payable on mortgage covered securities	**137,014**	195,121
Expenses	**1,928**	1,007
	138,942	196,128

19. Subordinated liabilities	**2009** **€ 000**	2008 € 000
Dated Capital Note (a)	**100,000**	100,000
Perpetual Capital Note (b)	**200,000**	200,000
	300,000	300,000

(a) €100,000,000 Dated Subordinated Capital Note – the loan to which this note relates was received from the parent company, Allied Irish Banks, p.l.c. ("AIB") on 13 February 2006. Interest on the amount of principle is calculated on a year of 360 days at a rate of 53 basis points over Euribor payable monthly in arrears. The Note has a fixed maturity date of 12 February 2031. Early repayment may occur at the option of AIB Mortgage Bank with the prior consent of the Central Bank and Financial Services Authority of Ireland (the "Central Bank") on any interest payment date falling any time after five years and one day from the date of issuing the Note.

The loan capital is unsecured and all rights and claims of AIB shall be subordinated to the claims of all creditors who are depositors or other unsubordinated creditors of AIB Mortgage Bank.

Notes to the accounts

19. Subordinated liabilities *(continued)*

(b) €200,000,000 Subordinated Perpetual Capital Note – the loan to which this note relates was received from AIB on 13 February 2006. Interest on the amount of principle is calculated on a year of 360 days at a rate of 100 basis points over Euribor payable monthly in arrears. The Note is undated and has no final maturity date but may be redeemed at the option of AIB Mortgage Bank with the prior consent of the Central Bank at any time after the fifth anniversary of its issue.

The loan capital is unsecured and all rights and claims of AIB shall be subordinated to the claims of all creditors who are depositors or other unsubordinated creditors of AIB Mortgage Bank and creditors of AIB Mortgage Bank whose claims are subordinated to the claims of depositors and other unsubordinated creditors of AIB Mortgage Bank but excluding Pari Passu Subordinated Creditors and those creditors of AIB Mortgage Bank whose claims rank or are expressed to rank junior to the claims of AIB.

20. Share capital	**2009** **€ 000**	2008 € 000
Authorised:		
1,000,000,000 ordinary shares of €1.00 each	**1,000,000**	1,000,000
Issued and fully paid:		
450,000,000 ordinary shares of €1.00 each (2008: 450,000,000 ordinary shares of €1.00 each)	**450,000**	450,000
Movements in issued share capital:		
At 1 January	**450,000**	425,000
New shares issued during the year	**-**	25,000
At 31 December	**450,000**	450,000

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

21. Capital Management

The AIB Group policy is to maintain adequate capital resources at all times, having regard to the nature and scale of its business and the risk inherent in its operations. It does this through an Internal Capital Adequacy Assessment Process ("ICAAP"). The overarching principle of the ICAAP is the explicit linkage between capital and risk; the adequacy of the Bank's capital is assessed on the basis of the risks it faces. This requires a clear assessment of the material risk profile of the Bank, and a consideration of the extent to which identified risks, both individually and in aggregate, requires capital to support them.

In addition, the level of capital held by the Bank is influenced by its minimum regulatory requirements.

Notes to the accounts

21. Capital Management *(continued)*

Capital resources and regulatory capital ratios
The table below shows AIB Mortgage Bank’s capital resources as at 31 December 2009 and 31 December 2008.

	Basel II	Basel II
	2009	2008
	€’000	€’000
Shareholders’ equity	**619,550**	537,040
Dated capital notes	**100,000**	100,000
Undated capital notes	**200,000**	200,000
Total capital resources	**919,550**	837,040

Capital resources increased by €82.5m during the year ended 31 December 2009. This increase arose as a result of net retentions of profit.

The Capital Requirements Directive (CRD) / AIB’s implementation of the CRD
The CRD introduces some significant amendments to the existing capital adequacy framework. Its goal is to provide a greater link between the risk a bank faces and the capital it requires and it does this in a number of ways. In terms of minimum capital requirements (‘Pillar 1’) it brings additional granularity in risk weightings under the foundation internal ratings based approach for credit risk, and introduces an explicit capital requirement for operational risk.

From 1 January 2008, the Bank has calculated its capital requirements under the CRD using the foundation internal ratings based approach.

	2009	2008
22. Dividend	**€ 000**	€ 000
Dividend Paid	-	70,000

No dividend has been recommended for approval, payable to the Bank’s parent company, Allied Irish Banks, p.l.c. at 31 December 2009.

23. Employee Information

For the year ended 31 December 2009 the average number of employees was 6 (2008: 6). As at 31 December 2009, the Bank had 6 employees.

Notes to the accounts

24. Statement of cash flow	**2009 € 000**	2008 € 000
Loans and receivables to Allied Irish Banks, p.l.c..	**840,138**	723,751
Cash and cash equivalents	**840,138**	723,751

"Cash and Cash Equivalents" are part of loans and receivables to banks in the Statement of Financial Position on page 23.

25. Auditor's remuneration	**2009 € 000**	2008 € 000
Auditor's remuneration		
Statutory audit	**67**	72
Audit related services	**13**	14
Total auditor's remuneration	**80**	86

Audit related services include fees for assignments which are of an audit nature.

26. Directors' remuneration	**2009 € 000**	2008 € 000
Fees	**42**	61
	42	61

27. Reporting currency

The currency used in these accounts is Euro which is denoted by 'EUR' or the symbol '€'.

28. Segmental Information

The Bank's income and assets are entirely attributable to mortgage lending activity in the Republic of Ireland.

29. Contingent liabilities and commitments

There were no contingent liabilities or assets at 31 December 2009 that would require disclosure under IAS 37 (2008: Nil).

At 31 December 2009 the Bank had €443m (2008: €679m) of approved mortgage loan applications that had not been drawn down as at the year end.

Notes to the accounts

30. Summary of the relationship of AIB Group with the Irish Government

In response to the decline in financial markets that began in 2008, the Irish Government took steps to stabilise the Irish banking industry and its participants, including the Group. These steps included:

(i) The Credit Institutions (Financial Support) Scheme 2008 (‘CIFS Scheme’);
(ii) The National Pension Reserve Fund Commission (“NPRFC”) Investment;
(iii) The Credit Institutions (Eligible Liabilities Guarantee) Scheme 2009 (‘ELG Scheme’); and
(iv) National Asset Management Agency (“NAMA”).

The actions set out above gave the Minister for Finance (‘the Minister’) and/or the Financial Regulator rights and powers over AIB (and other financial institutions) in respect of various matters including: (i) the acquisition of shares in any other credit institution or financial institution, or the establishment of subsidiaries or the acquisition of new business or businesses which would increase the liability of the Government under the guarantee; (ii) certain dated subordinated debt covered by the guarantee, including the maintenance of solvency ratios during the guarantee period; (iii) the preparation of a restructuring plan which, inter alia, assesses AIB’s viability over time; details how AIB intends to minimise and repay State Aid; and sets out how AIB will limit distortion of competition caused by the receipt of State Aid; (iv) the appointment of non-executive directors to its board (three such directors have been nominated by the Minister for Finance and appointed to the Board); (v) changes to the Board where the Board does not contain an appropriate balance between executive and non-executive directors; (vi) the appointment of persons to attend all meetings of the remuneration, audit, credit and risk committees of AIB; (vii) restructure its executive management responsibilities, strengthen its management capacity and improve its corporate governance; (viii) declaration and payment of dividends; (ix) restrictions in relation to directors’ and executives’ remuneration and termination payments; (x) buy-backs or redemptions of its shares; (xi) submission of reports and certificates of compliance with the CIFS scheme; (xii) the manner in which the Group extends credit to first time buyers of residential premises, small to medium enterprises (“SMEs”) and to other customers; and (xiii) restrictions over the manner in which AIB can deal with its NAMA assets.

The Financial Regulator, in consultation with the Minister, must impose conditions regulating the commercial conduct of AIB, having regard to capital ratios, market share and the Group’s balance sheet growth. AIB must take steps to comply with any liquidity, solvency and capital ratios that the Financial Regulator, following consultation with the Minister, may direct. AIB must comply with targets set for AIB by the Financial Regulator, in consultation with the Minister, such as loan/deposit targets and wholesale funding/total liabilities targets. AIB may also be required to limit its exposure to certain sectors, customers or connected persons where it is in the public interest and in the interests of financial stability and the maintenance of confidence in the banking system.

AIB has also agreed to consult with the Minister prior to taking any material action which may be reasonably expected to have a public interest dimension.

Further details of the financial support received from the Irish Government are set out in (i) to (iv) below.

(i) The Credit Institutions (Financial Support) Scheme 2008
The CIFS Scheme gives effect to the bank guarantee announced by the Irish Government on 30 September 2008. Under the CIFS Scheme, the Minister for Finance guarantees certain types of liabilities of certain participating institutions, including AIB and certain of its subsidiaries, for a two-year period from 30 September 2008. If AIB (including AIB Mortgage Bank) defaults in respect of a guaranteed liability during the period of the guarantee, the Minister commits to pay to the creditor an amount equal to that liability. There is no monetary cap on the guarantee and it covers all guaranteed liabilities of AIB (including AIB Mortgage Bank) which become due for payment up to 29 September 2010. AIB is obliged to pay a quarterly charge to the Irish Government for the guarantee.

Notes to the accounts

30. Summary of the relationship of AIB Group with the Irish Government *(continued)*

To progressively reduce the risk to the Exchequer under the guarantee, AIB must: (i) appropriately manage the Group's balance sheet in a manner consistent with the CIFS Scheme and the need to avoid significant distortion of financial flows; (ii) put in place improved structures to ensure long-term stability of funding; (iii) improve liquidity, solvency and capital ratios in circumstances where that is required; and (iv) take measures to minimise any risk of recourse to the guarantee as directed by the Governor of the Central Bank and the Financial Regulator, after consultation with the Minister.

If, in the opinion of the Minister, AIB is in breach of its obligations under the CIFS Scheme in a manner that is material in the context of the provisions of the guarantee, the Minister may increase the charge payable by AIB, impose additional unspecified conditions on AIB or revoke the guarantee (but may not do so retrospectively).

The Minister may revoke, in whole or in part, the guarantee to a participating institution in certain circumstances. If the Minister revokes the guarantee provided to AIB, all of AIB's fixed-term guaranteed liabilities outstanding at that time would nevertheless continue to have the full benefit of the guarantee up to 29 September 2010 or their maturity, whichever is earlier, and all guaranteed liabilities, including on-demand deposits, will be protected by notice of at least 90 days prior to any financial institution being removed from the CIFS Scheme.

(ii) National Pension Reserve Fund Commission ("NPRFC") Investment
On 13 May 2009, in implementing the Government's recapitalisation of AIB, the Group issued: (i) €3.5 billion of core tier 1 securities in the form of non-cumulative redeemable preference shares (the '2009 Preference Shares') and (ii) 294,251,819 warrants over ordinary shares (the '2009 Warrants'), to the NPRFC for an aggregate subscription price of €3.5 billion. The NPRF, the Government's national pensions reserve fund, is controlled by the NPRFC and managed by the National Treasury Management Agency ("NTMA").

(iii) The Credit Institutions (Eligible Liabilities Guarantee) Scheme 2009
On 21 January 2010, Allied Irish Banks, p.l.c., including its international branches and subsidiaries (which includes AIB Mortgage Bank) became participating institutions for the purposes of the Credit Institutions (Eligible Liabilities Guarantee) Scheme 2009, the ('ELG Scheme').

The ELG Scheme came into effect on 9 December 2009 and the National Treasury Management Agency was appointed the ELG scheme operator by the Minister for Finance. The ELG Scheme is intended to facilitate the ability of credit institutions in Ireland to issue debt securities and take deposits with a maturity after September 2010 on either a guaranteed or unguaranteed basis. All liabilities guaranteed under the CIFS Scheme as at the date an institution joins will remain unconditionally and irrevocably guaranteed under and in accordance with the terms of the CIFS Scheme. Eligible liabilities under the ELG Scheme comprise any of the following liabilities:
- all deposits (to the extent not covered by deposit protection schemes in Ireland (other than the CIFS Scheme) or in any other jurisdiction);
- senior unsecured certificates of deposit;
- senior unsecured commercial paper; and
- other senior unsecured bonds and notes.

Eligible liabilities must not have a maturity in excess of five years and must be incurred during the period from the commencement date of the ELG Scheme to 29 September 2010 (subject to six month review and approval under EU state aid rules).

From the time that a participating institution joins the proposed ELG Scheme, only covered liabilities of that participating institution (as defined in the CIFS Scheme) in existence or contracted for prior to that time will continue to be guaranteed under the CIFS Scheme. All such then-existing covered liabilities will remain guaranteed until 29 September 2010 under the CIFS Scheme.

Notes to the accounts

30. Summary of the relationship of AIB Group with the Irish Government *(continued)*

From the time that a participating institution joins the proposed ELG Scheme, any liabilities incurred or contracted for thereafter by that participating institution may be guaranteed under the ELG Scheme only.
The European Central Bank's pricing recommendations on government guarantees for bank debt dated 20 October 2008 will apply to liabilities guaranteed under the ELG scheme.

(iv) Participation in the National Asset Management Agency ("NAMA")
On 7 April 2009, the Minister for Finance announced the Government's intention to establish a national asset management agency. On 22 November 2009, the NAMA Act was enacted providing for the establishment of the National Asset Management Agency ("NAMA").The participation of AIB in the NAMA programme was approved by shareholders at an Extraordinary General Meeting held on 23 December 2009.The purposes of the NAMA Act include the restoration of stability to the banking system and the facilitation of restructuring of credit institutions of systemic importance to the Irish economy. Allied Irish Banks, p.l.c. and each of its subsidiaries, including AIB Mortgage Bank, was designated a participating institution under the Act on 12 February 2010. The consideration for the NAMA assets acquired from AIB will comprise the issue to AIB of NAMA bonds and subordinated NAMA bonds, the nominal value of which will be equal to the agreed purchase price of the NAMA Assets.

The AIB Group also submitted a restructuring plan to the European Commission, an unintended consequence of which involves the deferral of coupon payments on certain debt and equity instruments (see note 55 on Page 243 of Allied Irish Banks, p.l.c. financial statements).

Further details of the relationship with the Irish Government are set out in Note 55 in the Annual Report of Allied Irish Banks, p.l.c..

31. Related party transactions

(a) Transactions with Allied Irish Banks, p.l.c.

AIB Mortgage Bank is a subsidiary of Allied Irish Banks, p.l.c. ("AIB"). Banking transactions are entered into between AIB Mortgage Bank and AIB in the normal course of business. These include loans and deposits on an arms length basis. Interests paid to AIB and interests received from AIB are disclosed in Note 1 and Note 2 to the accounts. As at 31 December 2009, the total amounts of principal outstanding in respect of mortgage covered securities issued to Allied Irish Banks, p.l.c. was €5.7bn.

Most of the Bank's activities are outsourced to Allied Irish Banks, p.l.c. under an Outsourcing and Agency Agreement. Allied Irish Banks, p.l.c., as Service Agent for the Bank, originates residential mortgage loans through its retail branch network in the Republic of Ireland, services the mortgage loans and provides treasury services in connection with financing as well as a range of support services.

The Bank's activities are financed through the issuance of mortgage covered securities and a mortgage backed promissory note facility with the Central Bank, with the balance of funding being provided by Allied Irish Banks, p.l.c..

Notes to the accounts

31. Related party transactions *(continued)*

(b) Transactions with key management personnel

Loans to the Key Management Personnel, including executive and non-executive directors and senior executive officers, are made in the ordinary course of business on substantially the same terms, including interest rate and collateral, as those prevailing at the time for comparable transactions with other persons of similar standing not connected with AIB Mortgage Bank and do not involve more than the normal risk of collectability or present other unfavourable features. Loans to executive directors and senior executive officers are also made in the ordinary course of business, on terms available to other employees in the Bank generally, in accordance with established policy, within limits set on a case by case basis.

Details of loan facility transactions with key management personnel and connected parties, as appropriate, with AIB Mortgage Bank are as follows:

	Balance at 31 December 2008	Amounts advanced during 2009	Amounts repaid during 2009	Balance at 31 December 2009
	€'000	€'000	€'000	€'000
Kieran Crowley				
Loans	1,089	-	-	1,089
Interest charged during 2009	-	-	-	26
Maximum debit balance during 2009	-	-	-	1,089
Michael Keegan				
Loans	407	-	1	406
Interest charged during 2009	-	-	-	10
Maximum debit balance during 2009	-	-	-	407
David Kelly				
Loans	608	-	12	596
Interest charged during 2009	-	-	-	14
Maximum debit balance during 2009	-	-	-	608
Jennifer Winter				
Loans	103	-	11	92
Interest charged during 2009	-	-	-	2
Maximum debit balance during 2009	-	-	-	103

No other current or former Directors had loan facilities with AIB Mortgage Bank during the year ended 31 December 2009.

No impairment charges or provisions have been recognised in respect of any of the above loans or facilities and all interest that has fallen due has been paid.

Notes to the accounts

31. Related party transactions *(continued)*

(b) Transactions with key management personnel

	2009	2008
	€ 000	€ 000
Aggregate loan amounts outstanding at year end		
Directors	**2,183**	2,207
	2,183	2,207

32. Non adjusting events after the reporting period

No significant events have occurred in the period subsequent to the year end date and the date of approving the financial statements.

33. Approval of financial statements

The financial statements were approved by the Directors on 25 March 2010.