AIB Mortgage Bank

Directors' Report & Financial Statements

Year ended 31 December 2010

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Directors' report and financial statements

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Directors' and other information

Directors	Walter Brazil, Non-Executive Director Sean Cremen, Executive Director Seymour Cresswell, Executive Director Kieran Crowley, Independent Non-Executive Director Michael Keegan, Executive Director Jim Pender, Executive Director Catherine Woods, Independent Non-Executive Director
Registered office	Bankcentre Ballsbridge Dublin 4 Ireland
Secretary	David Schorman
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 annual report and financial statements for the year ended 31 December 2010. A statement of Directors' responsibilities in relation to the financial statements appears on page 12.

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' or the 'Group') and is regulated by the Central Bank of Ireland. 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. 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.

On 25 February 2011, Allied Irish Banks, p.l.c. transferred substantially all of its mortgage intermediary originated Irish residential loans, related security and related business to AIB Mortgage Bank. The aggregate principal amount outstanding of and accrued but unpaid interest on, the Irish residential loans transferred by Allied Irish Banks, p.l.c. to AIB Mortgage Bank on 25 February 2011 was approximately €4.2 billion. The transfer was effected pursuant to the statutory transfer mechanism provided for in the Asset Covered Securities Acts.

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. 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.

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

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.

AIB Group's corporate governance practices reflect Irish company law, the principles and provisions of the Combined Code on Corporate Governance ("the Combined Code") to 31 December 2010, and the UK Corporate Governance Code ("the UK Code") (introduced in June 2010 to apply to accounting periods beginning on or after 29 June 2010) with effect from 1 January 2011 and certain provisions of the US Sarbanes Oxley Act of 2002. In November 2010, the Central Bank of Ireland issued its Corporate Governance Code for Credit Institutions and Insurance Undertakings ("the Central Bank Code"), which came into effect from 1 January 2011 and imposes minimum core standards upon all credit institutions and insurance undertakings licensed or authorised by the Central Bank of Ireland.

AIB Group's corporate governance practices will henceforth also reflect the provisions of the Central Bank Code, including compliance with requirements which specifically relate to 'major institutions'.

Directors' Report

Principal activities *(continued)*
As a separately licensed Credit Institution, AIB Mortgage Bank's corporate governance practices will also henceforth reflect the relevant provisions of the Central Bank Code.

Governance is exercised through a Board of Directors and a senior management team. One of the conditions of the Bank's Central Bank licence requires that there should be a minimum of two Non-Executive Directors who are independent of the parent company. During 2010, the membership of the board of Allied Irish Banks, p.l.c. was subject to significant change which also impacted the board of AIB Mortgage Bank and as a result of which, during the period from 28 April to 31 December, the Bank was not in compliance with this condition. This position was subsequently rectified on 29 March 2011.

During 2010, the Board also included five Executive Directors, all of whom were directly involved in the operation of AIB Mortgage Bank, and two other directors, who while also employees of AIB, were deemed to be Non-Executive Directors by virtue of the roles they fulfill in areas of the organisation that are unrelated to the operations of AIB Mortgage Bank.

Business review
The economic environment in Ireland continues to be very challenging for the residential mortgage business. GDP declined by 1% in 2010 after a 7.6% decline in 2009. Unemployment increased from 11.8% at December 2009 to 13.6% at December 2010 (Source: Central Statistics Office). The peak (February 2007) to trough fall in house prices according to the ESRI/PTSB house price index was 38% up to December 2010. Many commentators however consider that this index understates or lags the underlying fall in house prices.

The Bank 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 wish to move house or top up their mortgage.

Total market mortgage drawdowns in Ireland were €4.7bn in 2010 compared with €8.1bn in 2009. Drawdowns in 2006, the peak year for drawdowns, were €39.9bn. (Source: Irish Mortgage Council). As a result the Bank's mortgage drawdowns were lower at €1.6bn in 2010 compared with €2.9bn in 2009. The Bank's mortgage portfolio before provisions decreased by 1% during 2010 to €20.5bn as at 31 December 2010 (2009: increase of 3.5% to €20.8bn as at 31 December 2009).

At 31 December 2010, the Mortgage Bank's mortgage portfolio (comprising substantially all branch originated loans but not AIB broker originated and staff loans) accounted for €20.5bn out of the total €27.2bn AIB Bank ROI residential mortgages, as reported in the Group's 2010 preliminary results announced on 12 April 2011.

The Mortgage Bank's portfolio comprises €14.2bn owner occupier and €6.3bn buy to let mortgages. Of the owner occupier portfolio, 54% are ECB tracker, 30% are on variable interest rates and 16% are fixed. 11% of the owner occupier portfolio are on interest only repayments. Of the buy to let portfolio, 63% are ECB tracker, 31% are on variable interest rates and 6% are fixed. 42% of the buy to let portfolio are on interest only repayments.

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

As a result of the increased pressure on borrowers repayment capacity and further decreases in property prices, impaired loans has increased to €839.5m, or 4.08% of total loans (2009: €381.7m or 1.84%). Provisions made for impaired loans in 2010 also increased significantly to €344.1m from €78.7m in 2009. As a result of the deterioration in the economy and the additional pressure on borrowers, Allied Irish Banks, p.l.c. has applied additional resources to its credit management function.

Directors' Report

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

Results for the year
The loss before taxation for 2010 was €316.5m, down from a profit before taxation of €94.3m in 2009, due mainly to an increase in provisions for impaired loans, loss on transfer of loans to NAMA and a provision for loans to be transferred to NAMA in 2011.

<u>Interest</u>
Net Interest income was €214.9m compared with €217.6m in 2009. The one month Euribor rate (the basis for most of the Bank's funding) was on average 0.44% below the ECB Refi rate (the basis for most of the Bank's customer pricing) in 2010 whereas it was on average 0.33% below it in 2009. This positive income impact was offset by higher cost of funding over one month Euribor, as funding for a portion of the mortgage book, other than covered bond funding, bore higher market funding costs.

Interest income on mortgage loans was €511.1m (2009: €528.5m), the decrease being largely due to a lower average ECB Refi rate in 2010 (average ECB Refi rate was at 1.0% in 2010 compared with 1.3% in 2009). In March 2010, the Owner Occupier Standard Variable Rate was increased by 0.50% and the Owner Occupier Loan to Value Variable Rate was increased by 0.34%. In August 2010, both the Owner Occupier Standard Variable Rate and the Owner Occupier Loan to Value Variable Rate were increased by 0.50%. Changes to Fixed Rates were also implemented in March and August 2010.

Interest income from deposits and interest rate swaps with Allied Irish Banks, p.l.c. was €228.4m (2009: €364.2m), the decrease resulting mainly from a decline in the 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 €313.6m (2009: €341.3m), the decrease being due to the lower one month Euribor interest rates. Interest payable to the Central Bank of Ireland in respect of the Mortgage-Backed Promissory Note facility and sale and repurchase agreements in respect of Self Issued Covered Bonds was €30.3m (2009: €32.1m) the reduction being mainly due to falling interest rates. Interest payable to holders of mortgage covered securities was €180.7m (2009: €301.7m), the decrease being mainly due to the lower average volume of external securities in issue and lower one month Euribor interest rates.

The trading gain of €0.8m (2009: loss €1.5m) resulted from changes in the fair value of interest rate swaps and certain related account items being hedged.

<u>NAMA transfer</u>
In accordance with eligibility terms prescribed by the National Asset Management Agency (NAMA), mortgages connected to qualifying land and development advances were transferred to NAMA during 2010. The fair value attaching to the transferred assets, based on the NAMA valuation process, generated a loss on transfer of €106.1m included under other operating expense. Further information is provided in Note 4 to the financial statements. In March 2011 a further transfer occurred of loans from AIB Mortgage Bank to NAMA resulting in a loss on transfer of €43.3m. As this transfer was deemed unavoidable at 31 December 2010 a provision of €43.9m has been recorded in the year end accounts for these loans as detailed in note 6.

<u>Credit provisions</u>
The provisions charge for impaired loans in 2010 was €344.1m, up from €78.7m in 2009. Provisions as at 31 December 2010 amounted to €441.5.m of which €160.6m were specific and €280.9m were Incurred But Not Reported ("IBNR").

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Directors' Report

Results for the year *(continued)*
Credit provisions *(continued)*
The increase in the IBNR provision was due to management's view of the heightened level of increased loss (not yet identified) in the book and the impact of more negative economic circumstances including employment and income levels. It takes into account the weaker credit performance of the Buy to Let portfolio compared to the Owner Occupier portfolio. It also reflects recent provision experience, the level of arrears, the level of requests for restructure, uncertainty over underlying peak to trough house price declines, the level of interest only mortgages and their maturity profile, and the level of negative equity.

Management's judgement in determining provisions has been informed by the results of the Central Bank of Ireland PCAR review announced on 31 March 2011.

Administrative expenses amounted to €37.5m (2009: €36.1m), and included €35.1m (2009: €33.2m) for services provided by Allied Irish Banks, p.l.c. under the Outsourcing and Agency Agreement.

Funding activities
During 2010, following the turmoil in the financial market experienced since August 2007, there has been some evidence of global recovery. However, Ireland and certain other European countries have been impacted by the continuing weakness in the banking sector and the sovereign debt crisis. The market for Irish bonds deteriorated throughout the year and in the third quarter of 2010 the Irish Government suspended bond sales.

While the Covered Bond market for core European countries has generally recovered, the Irish market has continued to deteriorate with the market remaining largely closed to new issuance and the secondary market not functioning properly.

In March and April 2010, AIB Mortgage Bank raised €25m of new Covered Bond funding from external investors under the Mortgage Covered Securities Programme. On 29 January 2010, the Bank redeemed a €2bn bond issued on 13 December 2006.

Under normal ECB open market operations, Covered Bonds including Irish Covered Bonds with appropriate ratings are accepted as collateral for sale and repurchase agreements, thus providing liquidity. AIB Mortgage Bank and Allied Irish Banks, p.l.c. used Covered Bonds issued internally within AIB as a source of such liquidity throughout the year.

At 31 December 2010, total covered bonds in issue amounted to €14.7bn (2009: €14.0bn), of which €2.8bn was issued to external debt investors, €5.8 billion was issued to Allied Irish Banks, p.l.c. and €6.1 billion was issued to AIB Mortgage Bank. The bonds issued to Allied Irish Bank, p.l.c. and to AIB Mortgage Bank were at 31 December 2010 held by the Central Bank of Ireland under sale and repurchase agreements.

The AIB Mortgage Bank Mortgage-Backed Promissory Note facility with the Central Bank of Ireland for normal ECB open market operations was used as a source of liquidity during the year with maximum drawdown of €1.5bn. As from 20 December 2010, this facility was no longer available due to a ratings downgrade by Moody's of Allied Irish Banks, p.l.c.. Accordingly, Nil was drawndown as at 31 December 2010, (31 December 2009: Nil).

The AIB Mortgage Bank Mortgage-Backed Promissory Note facility with the Central Bank of Ireland outside normal ECB open market operations has been used as a source of liquidity since November 2010. As at 31 December 2010, €0.9bn was drawn down maturing in January 2011 (31 December 2009: Nil drawdown).

The credit ratings for the Mortgage Bank's Covered Bond Programme deteriorated during 2010. A series of rating downgrades resulted in a loss of the AAA rating for the Covered Bond Programme, with Standard & Poor's being first to downgrade the Programme from AAA to AA+ on 11 October 2010. Fitch downgraded the Programme from AAA to A on 14 December 2010, and Moody's downgraded it from AAA to A2 on 20 December 2010.

Directors' Report

Funding activities *(continued)*
The current ratings as at 26 April 2011, for the Covered Bond Programme, Allied Irish Banks, p.l.c., and Ireland are shown below:

	AIB Mortgage Bank Covered Bond Programme	Allied Irish Banks p.l.c. Issuer default rating	Ireland (Sovereign)
Rating Agency			
Fitch	A	BBB	BBB+
Moody's	Baa3	Ba3	Baa3
Standard & Poor's	A	BB	BBB+

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 9 to the Financial Statements.

AIB Mortgage Bank is reliant on AIB Group for a) financing and b) the operation of a number of outsourced activities leading to significant uncertainties and reliance on the Group.
In summary, the AIB Group and as a result AIB Mortgage Bank considers the following risks and uncertainties to be the most material to its future performance:
- The economic environment in Ireland and the markets in which the Group operates continue to be very challenging.
- Constraints on liquidity and market reaction to factors affecting Ireland and the Irish economy have and continue to create an exceptionally challenging liquidity environment for the Group. Further downgrades to Irish sovereign ratings or the Group's credit ratings or outlook could limit the Group's access to funding, trigger additional collateral requirements and weaken its competitive position. Uncertainty over the terms of a further extension of the Eligible Liabilities Guarantee ("ELG") Scheme may expose the Group to further liquidity risks.
- Systemic Risks could disrupt the markets and impact the Group's financial condition and results of operations.
- Notwithstanding recent capital injections and the commitment of further capital, the Group is subject to the risk of having insufficient capital resources to meet increased minimum regulatory requirements.
- The Group remains subject to inherent risks concerning customer and counterparty credit quality and the actual or perceived failure or worsening creditworthiness of customers, other financial institutions and counterparties. In particular, pressure on personal income, employment levels, residential property values and the extent to which foreclosure becomes a prevalent feature of the market are sources of increased credit risk for the Group.
- The Group is subject to certain commitments and restrictions in relation to the operation of its business under various provisions of State support.
- Execution of the Restructuring Plan, including the disposal of assets as part of the deleveraging programme.
- The Group continues to face market risks, including non-trading interest rate risk, in the ordinary course of its business.
- The Group continues to face significant operational and reputational risks.
- The Group's businesses and financial condition could be affected by the fiscal, taxation, regulatory or other policies, laws and regulations and other actions of various governmental and regulatory authorities.
- The Group's deferred tax assets are substantially dependent on the generation of future profits over a number of years.

Share capital
The share capital of the Bank was €450m, being ordinary shares of €1 each, as at 31 December 2010. In addition, the Bank received a capital contribution of €80m from its parent Allied Irish Bank's p.l.c. as a result of the capital deficit arising from the loan provisions recorded in the financial statements to 31 December 2010.

AIB Mortgage Bank

Directors' Report

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 2010 and 31 December 2009.

	31 Dec 2010 €'000	31Dec 2009 €'000
Tier 1		
Paid up ordinary share capital	**450,000**	450,000
Capital contribution	**80,000**	-
Eligible reserves	**(107,362)**	119,868
Total tier 1 capital	**422,638**	569,868
Tier 2		
Subordinated perpetual loan capital	**200,000**	200,000
Subordinated term loan capital	**100,000**	100,000
Standardised IBNR and Excess IRB provisions	**45,272**	1,784
Total tier 2 capital	**345,272**	301,784
Gross capital		
Supervisory deductions	**-**	(77,115)
Total capital	**767,910**	794,537
Risk weighted assets		
On balance sheet	**6,074,571**	4,948,340
Off-balance sheet *	**28,546**	62,010
Total risk weighted assets	**6,103,117**	5,010,350
Capital ratios		
Tier 1	**6.69%**	10.98%
Total	**12.13%**	15.31%

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 2010, 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 8.1% as at 31 December 2010 (2009: 8.6%).

* See Note 33 to the financial statements for approved but undrawn mortgage loans, weighted at 6.7% under the CRD.

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.

AIB Mortgage Bank

Directors' Report

Going concern
The Mortgage Bank's activities are subject to risk factors. 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 15 to 17 and in note 9. 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.

The Bank's financial statements have been prepared on a going concern basis. It is however reliant on support from it's Parent, AIB. With respect to the Parent there are a number of material economic, political and market risks and uncertainties that impact the Irish Banking system which may cast significant doubt upon the Group's ability to continue as a going concern. In making its assessment of the Group's ability to continue as a going concern, the Board of Directors has taken into consideration the uncertainties that currently impact Irish financial institutions and the Group. These include the continuing ability to access funding from the Eurosystem funding and Central Bank of Ireland liquidity facilities to meet liquidity requirements and the commitment of the Government to provide the Group's required capital.

Notwithstanding these uncertainties, the Directors, having considered the statement to the Dail (the lower house of the Irish parliament) by the Minister for Finance ('the Minister') on 31 March 2011 and also the terms of the EU/IMF memorandum of understanding, are satisfied that it continues to be appropriate to prepare the financial statements of the Group on a going concern basis based on the following risk mitigants:

- the Government has indicated that it will ensure the Group is strongly capitalised, meeting a minimum level of 10.5% tier 1 capital in a base scenario and 6% in a stress scenario;
- the Group's access to liquidity and funding, particularly the availability of Eurosystem funding and Central Bank of Ireland liquidity facilities will enable it to meet its immediate and estimated funding requirements over the period; and
- the Government has acknowledged the Group's systemic importance and the actions of the Government to date indicate that it will continue to support the Irish financial system given its importance to the continued functioning of the Irish economy generally.

The continued deterioration of the Irish economy throughout 2010 has significantly and adversely affected the Group's financial condition and performance and presents significant risks and challenges for the Group in the years ahead. The downgrading of the Group and sovereign credit ratings, the withdrawal of the Irish Government from the funding markets, the EU/IMF Programme of Financial Support for Ireland and the consequent withdrawal of funds from Irish Banks have affected the Group's funding position in 2010. There is a significant ongoing liquidity challenge for the Group and for the Irish Banking system generally. These challenges have given rise to breaches of regulatory liquidity requirements in the latter part of 2010 and ongoing breaches in 2011. The downgrade in credit ratings and the risk of a further sovereign or Group downgrade has limited the Group's access to capital markets, as a result the Group has increased its recourse to Eurosystem financing facilities. At 31 December 2010, the Group had €25.2bn of collateralised funding from the European Central Bank and was accessing €11.4bn through non standard facilities with the Central Bank of Ireland. The Group expects that these facilities will continue to be available, if required, for the coming year.

On 31 March 2011, the Central Bank published the Financial Measures Programme Report which details the outcome of its review of the capital and funding requirements of domestic Irish Banks.

This programme aims to place the Irish Banking system in a position where it can fund itself and generate capital without undue reliance on the Irish and European public sectors, through a process of recapitalisation, deleveraging and reorganisation. Using a conservative approach, the Central Bank has set the following capital and liquidity requirements for the four banks examined under the programme.

Following the PCAR, AIB is required to raise €13.3bn in capital (€10.5bn plus a €2.8bn capital buffer). This latest PCAR announcement subsumes all previous PCARs and ensures AIB will have capital buffers well in excess of the minimum core tier 1 of 10.5% in a base case and of 6% in a stressed case.

Directors' Report

Going concern *(continued)*
The Credit Institutions (Stabilisation) Act 2010 was passed into law on 21 December 2010. The Act provides the legislative basis for the reorganisation and restructuring of the Irish Banking system agreed in the joint EU/IMF programme for Ireland. The Act applies to banks who have received financial support from the State, Building Societies and Credit Unions. The Group by way of the Government Guarantee and direct capital injection has received such support. The Act provides broad powers to the Minister (in consultation with the Governor of the Central Bank of Ireland) to act on financial stability grounds to effect the restructuring action and recapitalisation measures envisaged in the programme. This allows the Minister to take actions required to bring about a domestic retail banking system that is appropriate to and focused on the Irish economy.

The Board's requirement to consider the appropriateness of preparing the financial statements on the going concern basis has considered the Group's business and funding plans taking into account:

- The period over which the Irish economy is expected to recover from the current crisis;
- The implementation of joint EU/IMF programme for Ireland;
- The Group's schedule of committed debt repayments;
- The Group's ability to continue to access liquidity and funding, in particular from the Eurosystem and Central Bank of Ireland liquidity facilities;
- The ability of the Group to raise additional required capital in the financial markets, through other internal actions or failing that from the Irish Government to meet its required regulatory capital ratios: and
- The ability of the Group to dispose of assets and/or increase its deposit base to meet PLAR targets by the Central Bank of Ireland

The risks and uncertainties set out above and the options available to the Group have been considered by the Directors in concluding that it is appropriate to prepare the financial statements on a going concern basis.

On the basis of the continued availability of funding from Allied Irish Banks, p.l.c. to AIB Mortgage Bank the Directors of AIB Mortgage Bank 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 2010 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 2010**	1 January 2010*
Directors:		
Walter Brazil	**5,583**	5,583
Sean Cremen	**6,218**	6,218
Seymour Cresswell	**265**	1,808
Kieran Crowley	**12,520**	12,520
Michael Keegan	**5,645**	5,645
Jim Pender	**26,867**	26,867
Secretary:		
David Schorman	**8,453**	8,453

** or date of appointment, if later*

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 2010 are exercisable at various dates between 2011 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 2010	1 January 2010	Since 1 January, 2010 Granted	Since 1 January, 2010 Exercised	Price of options exercised	Market price at date of exercise	Weighted average subscription price of options outstanding at 31 December 2010
Directors:					€	€	€
Walter Brazil	**25,000**	25,000	-	-	-	-	13.15
Sean Cremen	**7,500**	7,500	-	-	-	-	13.24
Seymour Cresswell	**-**	-	-	-	-	-	-
Michael Keegan	**22,500**	22,500	-	-	-	-	13.24
Jim Pender	**-**	-	-	-	-	-	-
Secretary							
David Schorman	**2,000**	2,000	-	-	-	-	13.30

Independent Non-executive directors do not participate in 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. The conditional grants of awards outstanding at 31 December 2010 may wholly or partly vest in 2011, depending on the grant conditions being met.

	Total as at 31 December 2010	Lapsed during 2010	Granted during 2010	Total as at 1 January 2010*
Directors				
Walter Brazil	**16,310**	8,944	-	25,254
Seymour Cresswell	**-**	-	-	-
Sean Cremen	**-**	2,438	-	2,438
Michael Keegan	**16,968**	8,726	-	25,694
Jim Pender	**18,853**	10,253	-	29,106
Secretary:				
David Schorman	**-**	-	-	-

** or date of appointment, if later.*

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

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

There were no changes in the Directors' and Secretary's interests between 31 December 2010 and 26 April 2011. Ms. Catherine Woods was appointed to the Board on 29 March 2011. Her interest (inclusive of the interest of her spouse and minor children) in the Ordinary Shares of Allied Irish Banks, p.l.c. is nil.

AIB Mortgage Bank

Directors' Report

Directors and Secretary

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. Jennifer Winter resigned as a Non-Executive Director on 28 April 2010.
Mr. Sean Cremen was appointed Executive Director on 25 May 2010.
Mr. Maeliosa Ó hOgartaigh resigned as a Non-Executive Director and Deputy Chairman on 12 November 2010.
Mr. David Kelly resigned as Managing Director on 3 December 2010.
Ms. Catherine Woods was appointed Independent Non-Executive Director on 29 March 2011.
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, other than those disclosed in note 36 of the financial statements (i.e. transfer of intermediary mortgage portfolio, share capital injections and NAMA transfer) 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

Director Catherine Woods

Director Walter Brazil

26 April 2011

AIB Mortgage Bank

Statement of Directors' responsibilities in relation to the Financial Statements

Company law requires the Directors to prepare financial statements for each financial year. Under that law 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 as adopted by the EU to present fairly the financial position and performance of the Bank; the Companies Acts 1963 to 2009 provide in relation to such financial statements that references in the relevant part of the Act and 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;
- state that the financial statements comply with IFRS as adopted by the EU as applied in accordance with the Companies Acts 1963 to 2009; 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.

On behalf of the Board

Director Catherine Woods

Director Walter Brazil

26 April 2011

AIB Mortgage Bank

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 2010 which comprise the Income Statement, the Statement of Comprehensive Income, the Statement of Financial Position, the Statement of Cash Flows, 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) both as issued by the IASB and subsequently adopted by the EU are set out in the Statement of Directors’ Responsibilities on page 12.

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 both as issued by the IASB and subsequently 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.

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.

Basis of audit opinion *(continued)*

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 both as issued by the IASB and subsequently adopted by the EU, of the state of the Bank's affairs as at 31 December 2010 and of its loss for the year then ended; and

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

Emphasis of matter
In forming our opinion on these financial statements, which is not qualified, we have considered the adequacy of the disclosures in the Basis of Preparation on page 15 to the financial statements concerning the Bank's ability to continue as a going concern. These disclosures set out the dependence of the Bank on its Parent for capital and funding support and the position of its Parent given the material economic, political and market risks and uncertainties that impact the Irish banking system. These include the Parent's continued ability to access funding from the Eurosystem and the Irish Central Bank to meet its liquidity requirements. These conditions together with the other matters mentioned in the Basis of Preparation indicate the existence of a material uncertainty which may cast significant doubt about the Bank's ability to continue as a going concern. The financial statements do not include the adjustments that would result if the Bank was not a going concern.

Other matters
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 2010 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 *26 April 2011*
Registered Auditor
Chartered Accountants
1 Harbourmaster Place
International Financial Services Centre
Dublin 1

AIB Mortgage Bank

Accounting policies

The accounting policies applied in the preparation of the financial statements for the year ended 31 December 2010 are set out below. There are no significant changes to the accounting policies described on pages 12 to 21 in the 2009 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 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 subsequently adopted by the European Union ("EU") and applicable for the year ended 31 December 2010. The accounting policies have been consistently applied by the Bank and are consistent with the previous year, unless otherwise described. The financial statements also comply with the requirements of Irish Statute comprising the Companies Acts 1963 to 2009, the Asset Covered Securities Acts 2001 and 2007 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.

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 loan impairment; determination of the fair value of certain financial instruments and the recoverability of deferred tax. A description of these estimates and judgements is set out in section 17 of the accounting policies.

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 Bank 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.

There are a number of material economic, political and market risks and uncertainties that impact the Irish Banking system which may cast significant doubt upon the Group's and as a result the Bank's ability to continue as a going concern. In making its assessment of the Group's ability to continue as a going concern, the Board of Directors has taken into consideration the uncertainties that currently impact Irish financial institutions and the Group. These include the continuing ability to access funding from the Eurosystem funding and Central Bank of Ireland liquidity facilities to meet liquidity requirements and the commitment of the Government to provide the Group's required capital.

Notwithstanding these uncertainties, the Directors, having considered the statement to the Dail (the lower house of the Irish parliament) by the Minister for Finance ('the Minister') on 31 March 2011 and also the terms of the EU/IMF memorandum of understanding, are satisfied that it continues to be appropriate to prepare the financial statements of the Group on a going concern basis based on the following risk mitigants:

- the Government has indicated that it will ensure the Group is strongly capitalised, meeting a minimum level of 10.5% tier 1 capital in a base scenario and 6% in a stress scenario;
- the Group's access to liquidity and funding, particularly the availability of Eurosystem funding and Central Bank of Ireland liquidity facilities will enable it to meet its immediate and estimated funding requirements over the period; and
- the Government has acknowledged the Group's systemic importance and the actions of the Government to date indicate that it will continue to support the Irish financial system given its importance to the continued functioning of the Irish economy generally.

The continued deterioration of the Irish economy throughout 2010 has significantly and adversely affected the Group's financial condition and performance and presents significant risks and challenges for the Group in the years ahead. The downgrading of the Group and sovereign credit ratings, the withdrawal of the Irish Government from the funding markets, the EU/IMF Programme of Financial Support for Ireland and the consequent withdrawal of funds from Irish Banks have affected the Group's funding position in 2010. There is a significant ongoing liquidity challenge for the Group and for the Irish Banking system generally. These challenges have given rise to breaches of regulatory liquidity requirements in the later part of 2010 and ongoing breaches in 2011. The downgrade in credit ratings and the risk of a further sovereign or Group downgrade has limited the Group's access to capital markets and as a result the Group has increased its recourse to Eurosystem financing facilities. At 31 December 2010, the Group had €25.2bn of collateralised funding from the European Central Bank and was accessing €11.4bn through non standard facilities with the Central Bank of Ireland. The Group expects that these facilities will continue to be available, if required, for the coming year.

On 31 March 2011, the Central Bank published the Financial Measures Programme Report which details the outcome of its review of the capital and funding requirements of domestic Irish Banks.

This programme aims to place the Irish Banking system in a position where it can fund itself and generate capital without undue reliance on the Irish and European public sectors, through a process of recapitalisation, deleveraging and reorganisation. Using a conservative approach, the Central Bank has set the following capital and liquidity requirements for the four banks examined under the programme.

Following the PCAR, AIB is required to raise €13.3bn in capital (€10.5bn plus a €2.8bn capital buffer). This latest PCAR announcement subsumes all previous PCARs and ensures AIB will have capital buffers well in excess of the minimum core tier 1 of 10.5% in a base case of 6% in a stressed case.

Accounting policies

3. Basis of preparation *(continued)*

Going Concern (continued)

The Credit Institutions (Stabilisation) Act 2010 was passed into law on 21 December 2010. The Act provides the legislative basis for the reorganisation and restructuring of the Irish Banking system agreed in the joint EU/IMF programme for Ireland. The Act applies to banks who have received financial support from the State, Building Societies and Credit Unions. The Group by way of the Government Guarantee and direct capital injection has received such support. The Act provides broad powers to the Minister (in consultation with the Governor of the Central Bank of Ireland) to act on financial stability grounds to effect the restructuring action and recapitalisation measures envisaged in the programme. This allows the Minister to take actions required to bring about a domestic retail banking system that is appropriate to and focused on the Irish economy.

The Board's requirement to consider the appropriateness of preparing the financial statements on the going concern basis has considered the Group's business and funding plans taking into account:

- The period over which the Irish economy is expected to recover from the current crisis;
- The implementation of joint EU/IMF programme for Ireland;
- The Group's schedule of committed debt repayments;
- The Group's ability to continue to access liquidity and funding, in particular from the Eurosystem and Central Bank of Ireland liquidity facilities;
- The ability of the Group to raise additional required capital in the financial markets, through other internal actions or failing that from the Irish Government to meet its required regulatory capital ratios: and
- The ability of the Group to dispose of assets and/or increase its deposit base to meet PLAR targets by the Central Bank of Ireland

The risks and uncertainties set out above and the options available to the Group have been considered by the Directors in concluding that it is appropriate to prepare the financial statements on a going concern basis.

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 amendments to standards have been adopted by the Bank during the year ended 31 December 2010:

<u>Amendments to IAS 24 – Related Parties Disclosures</u>

As permitted in the amendment, the Bank has partially early adopted the exemption for government-related entities included within the amendment to IAS 24-Related Parties Disclosures. This exemption removes the requirement for government-related entities to disclose details of all transactions with the Government and other government-related entities.

The amendment to this standard requires the reporting entity to disclose the following information about the transactions and related outstanding balances, as set out in the revised standard:

- the name of the government and the nature of its relationship with the reporting entity (i.e. control, joint control or significant influence).

The following information in sufficient detail:

- the nature and amount of each individually significant transaction;
- for other transactions that are collectively, but not individually significant, a qualitative or quantitative indication of their extent.

The Bank has not early adopted other aspects of the amendment to IAS 24 that revise the definition of related parties. Therefore, the disclosures relating to other (non-government) related parties is provided on the same basis as in prior years.

Accounting policies

3. Basis of preparation *(continued)*
Amendments to IAS 39 Financial Instruments: Recognition and Measurement – Eligible Hedged Items
The amendments clarify the application of existing principles that determine whether specific risks or portions of cash flows are eligible for designation in a hedging relationship. The application of the amendments did not have any impact on the Bank's financial statements in 2010.

Improvements to IFRSs
The IASB issued 'Improvements to IFRSs' in both May 2008 and in April 2009, which comprise a collection of necessary but not urgent amendments to IFRSs. The adoption of the following amendments resulted in changes to accounting policies but did not have any material impact on the financial position or performance of the Bank for the year ended 2010:

Issued in April 2009
IAS 7 Statement of Cash Flows: This amendment which is effective for annual periods beginning on or after 1 January 2010, states that only expenditure that results in recognising an asset can be classified as a cash flow from investing activities.

IAS 36 Impairment of Assets: The amendment which has been applied prospectively from 1 January 2010 clarifies that the largest unit permitted for allocating goodwill acquired in a business combination, is the operating segment as defined in IFRS 8 before aggregation for reporting purposes.

Other amendments resulting from Improvements to IFRSs which the Bank adopted 2010 did not have any impact on the accounting policies, financial position or performance of the Bank.

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.

Accounting policies

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.

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.

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

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

Accounting policies

9. Derivatives and hedge accounting *(continued)*
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.

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.

Accounting policies

10. Non-current assets held for sale *(continued)*
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.

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 7). 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 4). The impairment policy for loans and receivables as set out in accounting policy number 12 continues to apply.

However, where the transfer of loans to NAMA is deemed to be unavoidable and the discount pertaining to the transfer has been practically accepted by the Bank, a provision is made for a constructive obligation and reported as a 'provision for liabilities and commitments' in both the Income Statement and the Statement of Financial Position.

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 less any amount previously provided and consideration received will be recognised in the Income Statement as a gain or loss in other operating income.

Other loans (currently designated as NAMA 2 by the Bank) that may transfer to NAMA during 2011, are accounted for as 'loans and receivables to customers' due to:
- the lack of clarity over the loans to be transferred;
- the discount to be applied; and
- the fact that legislation dealing with any possible transfer had not been enacted at 31 December 2010.

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.

Impairment
The Bank assesses at each reporting date 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;

Accounting policies

12. Impairment of financial assets *(continued)*
Impairment (continued)

(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.

Incurred but not reported
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.

Impairment loss
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 is included in the income statement.

When a loan has been subjected 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.

Past due loans
When a borrower fails to make a contractually due payment, a loan is deemed to be past due. 'Past due days' is the term used to describe the cumulative numbers of days that a missed payment is overdue. Past due days commence from the close of business on the day on which a payment is due but not received.

Loans and receivables renegotiated
Loans and receivables renegotiated are those facilities outstanding at the reporting date that, during the financial year have had their terms renegotiated, resulting in an upgrade from 91+ days past due or impaired status to performing status.

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

Accounting policies

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. Income tax, including deferred tax
Income tax comprises current and deferred tax. Income 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.

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

Deferred and current tax assets and liabilities are only offset when they arise in the same tax reporting group and where there is both the legal right and the intention to settle the current tax assets and liabilities on a net basis or to realise the asset and settle the liability simultaneously.

Income tax payable on profits, based on the applicable tax law in each jurisdiction, is recognised as an expense in the period in which the profits arise. The tax effects of income tax losses available for carry forward are recognised as an asset when it is probable that future taxable profits will be available against which these losses can be utilised.

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.

Accounting policies

17. Accounting estimates and judgements *(continued)*
(a) Loan impairment *(continued)*
A specific provision is made against problem loans when, in the judgement of management, the estimated repayment realisable from the obligor, including the value of any security available, is likely to fall short of the amount of principal and interest outstanding on the obligor's loan account. The amount of the specific provision made in the Bank's financial statements is intended to cover the difference between the assets carrying value and the present value of estimated future cash flows discounted at the assets original effective interest rates. 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.

(c) Deferred tax
Deferred income tax is provided, using the financial statement liability method, on temporary differences between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred income tax is determined using tax rates based on legislation enacted or substantively enacted at the reporting date and expected to apply when the deferred tax asset is realised or the deferred tax liability is settled.

Accounting policies

17. Accounting estimates and judgements *(continued)*
(c) Deferred tax *(continued)*
Deferred income tax assets are recognised where it is probable that future taxable profits will be available against which the temporary differences will be utilised.

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

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.

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 2011.

The IASB issued 'Improvements to IFRSs in May 2010, which comprise a collection of necessary but not urgent amendments to IFRSs. The amendments have not been adopted as they become effective for annual periods on or after either 1 July 2010 or 1 January 2011. These amendments are not expected to have a material impact on the Bank's financial statements.

The following will be applied in 2011:

<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 which, as permitted by the amendment, has been early adopted by the Bank in 2010. The remainder of the amendment will impact upon the disclosure of certain 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 which is effective for annual reports beginning on or after 1 February 2010, 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.

Accounting Policies

20. Prospective accounting changes *(continued)*

IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments
This IFRIC which is effective for annual periods beginning on or after 1 July 2010, 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.

Amendments to IFRS 7 – Financial Instruments: Disclosures
The amendment to IFRS 7 clarifies the required level of disclosure about credit risk and collateral held and provides relief from disclosures previously required regarding renegotiated loans.

The following will be applied in 2012:

Amendments to IFRS 7 –Disclosures – Transfers of Financial Assets
These amendments which are effective for annual periods beginning on or after 1 July 2011, comprise additional disclosures on transfer transactions of financial assets (for example securitisations), including possible effects of any risks that may remain with the transferor or the assets. Additional disclosures are also required if a disproportionate amount of transfer transactions are undertaken around the end of a reporting period. These amendments have been approved by the IASB, but have yet to be endorsed by the EU. The impact on the Bank will be dependent on any such future financial assets transfers.

The following will be applied in 2013 subject to EU endorsement:

IFRS 9 Financial Instruments
Phase 1: Classification and measurement
In November 2009, the IASB issued IFRS 9 'Financial Instruments', effective for accounting periods beginning on or after 1 January 2013, to address the classification and measurement of financial assets. This is the first phase of its project to replace IAS 39 and simplify the accounting for financial instruments.

The new standard endeavours to enhance the ability of investors and other users of financial information to understand the accounting for financial assets and to reduce complexity. IFRS 9 uses a single approach to determine whether a financial asset is measured at amortised cost or fair value, replacing the many different rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments (its business model) and the contractual cash flow characteristics of the financial assets.

On 28 October 2010, the IASB reissued IFRS 9, incorporating new requirements on accounting for financial liabilities, and carrying over from IAS 39 the requirements for derecognition of financial assets and financial liabilities.
- IFRS 9 doesn't change the basic accounting model for financial liabilities under IAS 39. Two measurement categories continue to exist: fair value through profit or loss ("FVTPL") and amortised cost. Financial liabilities held for trading are measured at FVTPL, and all other financial liabilities are measured at amortised cost unless the fair value option is applied.
- The basic premise for the derecognition model in IFRS 9 (carried over from IAS 39) is to determine whether the asset under consideration for derecognition is:
    - an asset in its entirety or
    - specifically identified cash flows from an asset (or a group of similar financial assets) or
    - a fully proportionate (pro rata) share of the cash flows from an asset (or a group of similar financial assets), or
    - a fully proportionate (pro rata) share of specifically identified cash flows from a financial asset (or a group of similar financial assets)
- A financial liability should be removed from the statement of financial position when, and only when, it is extinguished, that is, when the obligation specified in the contract is either discharged or cancelled or expires.

Accounting Policies

20. Prospective accounting changes *(continued)*
IFRS 9 Financial Instruments *(continued)*
- All derivatives, including those linked to unquoted equity investments, are measured at fair value. Value changes are recognised in profit or loss unless the entity has elected to treat the derivative as a hedging instrument in accordance with IAS 39, in which case the requirements of IAS 39 apply.

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

Phase 2: Impairment of financial assets
Subsequent to the issue of IFRS 9 in November 2009, the IASB issued an exposure draft of its proposals for changes to the impairment rules for financial assets measured at amortised cost. The proposals are intended to result in the earlier recognition of impairment losses. The model proposed in the exposure draft is an 'expected loss model'. Under that model, expected losses are recognised throughout the life of a loan or other financial asset measured at amortised cost, not just after a loss event has been identified. The expected loss model avoids what many see as a mismatch under the incurred loss model – front-loading of interest revenue (which includes an amount to cover the lender's expected loan loss) while the impairment loss is recognised only after a loss event occurs.

This exposure draft is expected to be incorporated into IFRS 9 with the effective date currently set at January 2013 with comparative information required.

Phase 3: Hedge accounting
In December 2010 the IASB issued an exposure draft on hedge accounting which will ultimately be incorporated into IFRS 9. The exposure draft proposes a model for hedge accounting that aims to align accounting with risk management activities. It is proposed that the financial statements will reflect the effect of an entity's risk management activities that uses financial instruments to manage exposures arising from particular risks that could affect profit or loss. This aims to convey the context of hedge instruments to allow insight into their purpose and effect.

It is expected by the end of June 2011, then, IFRS 9 will be a complete replacement for IAS 39. Whilst the impacts on Bank reporting are expected to be significant, these have not yet been determined.

IFRS Practice Statement – Management Commentary
In December 2010, the IASB issued the IFRS Practice Statement *Management Commentary*. The Practice Statement provided a broad, non-binding framework for the presentation of management commentary and is designed to promote good practice in financial reporting and to promote comparability across entities that present management commentary.

The objective of the Practice Statement is to assist management in presenting useful *management commentary* that relates to financial statements that have been prepared in accordance with IFRSs.

AIB Mortgage Bank

Income statement
for the year ended 31 December 2010

	Notes	**31 Dec 2010 € 000**	31 Dec 2009 € 000
Interest and similar income	1	**739,478**	892,704
Interest expense and similar charges	2	**(524,588)**	(675,067)
Net interest income		**214,890**	217,637
Trading gain/ (loss)	3	**752**	(1,472)
Other operating income		**131**	4
Other operating expense	4	**(106,680)**	(7,106)
Total operating income		**109,093**	209,063
Administrative expenses	5	**(37,518)**	(36,102)
Operating profit before provisions		**71,575**	172,961
Provisions for liabilities and commitments	6	**(43,905)**	-
Provisions for impairment of loans and receivables	7	**(344,141)**	(78,664)
Operating (loss) / profit before taxation		**(316,471)**	94,297
Taxation on ordinary activities	8	**39,559**	(11,787)
(Loss) / profit for the year		**(276,912)**	82,510

The operating profit arises from continuing operations.

The notes on pages 33 to 72 are an integral part of these financial statements.

Director Catherine Woods *Director* Michael Keegan

Director Walter Brazil *Secretary* David Schorman

26 April 2011

Statement of comprehensive income
for the year ended 31 December 2010

	31 Dec 2010 € 000	31 Dec 2009 € 000
(Loss)/ profit for the year	**(276,912)**	82,510
Other comprehensive income	-	-
Total comprehensive income for the year	**(276,912)**	82,510

AIB Mortgage Bank

Statement of financial position

as at 31 December 2010

	Notes	31 Dec 2010 € 000	31 Dec 2009 € 000
Assets			
Balances at central bank		**50**	50
Loans and receivables to banks	11	**16,470,576**	18,208,051
Loans and receivables to customers	12	**20,074,375**	20,692,512
Other assets	14	**24,324**	23,328
Deferred taxation	15	**39,559**	-
Derivative financial instruments	10	**290,640**	268,351
Financial assets held for sale to NAMA	16	**77,791**	115,008
Assets classified as held for sale	17	**5,203**	1,184
Total assets		**36,982,518**	39,308,484
Liabilities			
Deposits by central banks and banks[1]	18	**27,332,549**	27,474,129
Customer accounts		**26**	175
Derivative financial instruments	10	**3,126**	3,585
Debt securities in issue	19	**8,807,075**	10,760,078
Current taxation		**-**	11,787
Other liabilities		**380**	238
Accruals and deferred income	20	**72,296**	138,942
Subordinated liabilities	21	**300,000**	300,000
Provisions for liabilities and commitments	22	**44,428**	-
Total liabilities		**36,559,880**	38,688,934
Shareholders' equity			
Share capital	23	**450,000**	450,000
Capital reserves	24	**80,000**	**-**
Profit and loss account		**(107,362)**	169,550
Total shareholders' equity		**422,638**	619,550
Total liabilities and shareholders' equity		**36,982,518**	39,308,484

[1] This includes €2.75bn of Central Bank borrowings (2009: €1.5bn)

Director Catherine Woods *Director* Michael Keegan

Director Walter Brazil *Secretary* David Schorman

26 April 2011

AIB Mortgage Bank

Statement of cash flows

for the year ended 31 December 2010

	Notes	**31 Dec 2010 € 000**	31 Dec 2009 € 000
Reconciliation of profit before taxation to net cash inflow from operation activities			
(Loss) / profit before taxation		**(316,471)**	94,297
(Increase)/ decrease in prepayments and accrued income		**(997)**	11,768
(Decrease) in accruals and deferred income		**(66,646)**	(57,186)
(Decrease) in customer accounts		**(149)**	(59)
Decrease / (increase) in loans and receivables to customers		**617,887**	(704,361)
Decrease/ (increase) in assets held for sale		**33,198**	(116,192)
(Decrease) in debt securities in issue		**(1,953,003)**	(2,408,880)
(Increase) in derivative financial instruments		**(22,748)**	(24,648)
Decrease/ (increase) in loans and receivables to Allied Irish Banks, p.l.c.		**1,817,475**	(973,620)
(Decrease) / increase in loans and receivables from Allied Irish Banks, p.l.c.			**(141,580)**
	4,291,475		
Decrease in other assets		-	111
Increase in other liabilities		**142**	17
Increase in balances at central bank		-	(25)
Increase in provisions for liabilities and commitments		**44,428**	**-**
Net cash inflow from operating assets and liabilities		**11,536**	112,697
Net cash inflow from operating activities before taxation		**11,536**	112,697
Taxation paid		**(11,787)**	-
Taxation refund		**-**	3,690
Net cash outflow/inflow from operating activities		**(251)**	116,387
(Decrease) /increase in cash and cash equivalents		**(251)**	116,387
Opening cash and cash equivalents		**840,138**	723,751
Closing cash and cash equivalents	28	**839,887**	840,138

Statement of changes in equity
for the year ended 31 December 2010

	Share capital € 000	Capital reserves € 000	Profit and loss account € 000	Total € 000
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
Balance at 1 January 2010	**450,000**	**-**	**169,550**	**619,550**
Loss attributable to equity holders	-	-	**(276,912)**	**(276,912)**
Capital contribution received	-	**80,000**	-	**80,000**
Balance at 31 December 2010	**450,000**	**80,000**	**(107,362)**	**422,638**

Notes to the accounts

1. Interest and similar income	2010 € 000	2009 € 000
Interest on loans and receivables to customers	**511,120**	528,467
Interest receivable from Allied Irish Banks, p.l.c.	**228,358**	364,237
	739,478	892,704

Interest receivable from Allied Irish Banks, p.l.c. includes net interest receivable of €110m on derivatives.
All income earned derives from activities carried out in the Republic of Ireland.

2. Interest expense and similar charges	2010 € 000	2009 € 000
Interest payable to Allied Irish Banks, p.l.c.	**313,622**	341,313
Interest on debt securities in issue	**180,705**	301,683
Interest on amounts due to the Central Bank of Ireland	**30,261**	32,071
	524,588	675,067

Included within the interest payable to Allied Irish Banks, p.l.c. is €6.7m (2009: Nil) in respect of the Irish Government's Eligible Liability Guarantee ("ELG") scheme which is allocated to AIB Mortgage Bank. AIB Mortgage Bank covered bonds are excluded from the scheme however a charge is allocated due to the usage by AIB Mortgage Bank of long term senior debt in its funding mix

3. Trading gain/ (loss)	2010 € 000	2009 € 000
Trading gain/ (loss)	**752**	(1,472)

Changes in fair value of interest rate swaps, and certain related account items being hedged, resulted in a trading gain of €0.8m (2009: €1.5m loss). A gain of €0.5m (2009: €1.9m 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 €0.3m (2009: €0.4m gain), 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	2010 € 000	2009 € 000
Fee payable under Government guarantee scheme	**549**	7,106
Loss on transfer of financial instruments held for sale to NAMA	**106,131**	-
	106,680	7,106

The fee payable reflects the charge in respect of the Irish Government's Credit Institutions (Financial Support) ("CIFs") scheme. The CIFs scheme expired on 29th September 2010.

Loss on transfer of financial instruments held for sale to NAMA
At 31 December 2009, certain financial assets and liabilities (mainly loans and receivables) were classified as held for sale to NAMA. By 31 December 2010 the transfer of financial assets to NAMA was substantially complete. A loss arose on the transfer due to NAMA acquiring these instruments at a discount to their carrying value. The loss on transfer for the Mortgage Bank is recorded within other operating expense in the income statement.

The table below sets out the loss on transfer of financial instruments to NAMA.

	2010 € 000
Gross carrying value of loans transferred to NAMA	**214,021**
Specific provisions	**(11,242)**
Net loans	**202,779**
Accrued interest and other	**(1,361)**
Net carrying value of financial instruments transferred	**201,418**

The following table sets out details of the individual tranches of loans that transferred to NAMA.

	Date of transfer	**Net carrying value**	**Fair value of consideration**	**Loss on disposal**	**Discount %**
Tranche 1	6 April 2010	6,637	5,623	1,014	15
Tranche 2	12 July 2010	10,558	8,601	1,957	19
Tranche 3	5 November 2010	17,236	10,985	6,251	36
Tranche 4	17 December 2010	166,987	70,078	96,909	58
Total		**201,418**	**(95,287)**	**106,131**	**53**

Notes to the accounts

4. Other operating expense *(continued)*	**2010 € 000**

The following table analyses the overall impact in the income statement of financial instruments, both transferred and held for sale to NAMA*

Included in	
Loss on transfer of financial instruments held for sale to NAMA	**(106,131)**
Provisions for impairment of loans and receivables	**(530)**
Provisions for liabilities and commitments (note 6)	**(43,905)**

*Excludes amounts relating to interest income, related funding and other income on the underlying financial instruments.

5. Administrative expenses	**2010 € 000**	2009 € 000
Personnel expenses		
Wages and salaries	**346**	361
Social security costs	**36**	39
Retirement benefits	**50**	65
Other personnel expenses	**7**	15
	439	480
Other administrative expenses	**1,962**	2,409
Amounts payable to Allied Irish Banks, p.l.c. under the Outsourcing and Agency Agreement	**35,117**	33,213
	37,518	36,102

6. Provisions for liabilities and commitments	**2010 € 000**	2009 € 000
Provision for loss on transfer of loans to NAMA	**43,905**	-
	43,905	-

At 31 December 2010, the transfer of certain loans to NAMA was deemed unavoidable and accordingly a provision of €43.9m, being a constructive obligation, was made for the expected discount determined to be 60 per cent on a gross carrying value of loans amounting to €77.8m. The financial assets held for sale to NAMA at 31 December 2010 were transferred to NAMA in March 2011 resulting in a loss of €43.3m.

Notes to the accounts

7. Provisions for impairment of loans and receivables

	2010			2009		
	Specific	**IBNR**	**Total**	Specific	IBNR	Total
	€ 000	**€ 000**	**€ 000**	€ 000	€ 000	€ 000
Balance at start of year	**67,703**	**48,507**	**116,210**	22,146	18,397	40,543
Charge against income statement	**111,741**	**232,400**	**344,141**	48,304	30,360	78,664
Transfer to assets held for sale to NAMA	**-**	**-**	**-**	(2,352)	(250)	(2,602)
Transfer to assets classified as held for sale	**-**	**-**	**-**	(395)	-	(395)
Provisions on loans and receivables transferred to NAMA	**(11,242)**	**-**	**(11,242)**	**-**	**-**	**-**
Amounts written off	**(7,634)**	**-**	**(7,634)**	**-**	**-**	**-**
At end of year	**160,568**	**280,907**	**441,475**	67,703	48,507	116,210

By geographic location and industry sector

	2010	2009
	€ 000	€ 000
Republic of Ireland		
Home mortgages	**441,475**	116,210
	441,475	116,210

8. Taxation

	2010	2009
	€ 000	€ 000
Corporation tax		
Current tax on loss for the period (2009: €94.3m @ 12.5%)	-	11,787
Deferred taxation		
Origination of temporary differences (see note 15)	**(39,559)**	-
Total income tax	**(39,559)**	11,787

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

Notes to the accounts

9. 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.

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 AIB Group, 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.

Notes to the accounts

9. Risk management *(continued)*

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.

Maximum exposure to credit risk

			2010			2009
	Amortised cost	**Fair value**	**Total**	Amortised cost	Fair value	Total
	€ 000	**€ 000**	**€ 000**	€ 000	€ 000	€ 000
Balances at central banks	**50**	-	**50**	50	-	50
Derivative financial instruments		**290,640**	**290,640**	-	268,351	268,351
Loans and receivables to banks	**16,470,576**	**-**	**16,470,576**	18,208,051	-	18,208,051
Loans and receivables to customers	**20,074,375**	-	**20,074,375**	20,692,512	-	20,692,512
Deferred taxation	**39,559**	**-**	**39,559**			
Assets classified as held for sale	**5,203**	-	**5,203**	1,184	**-**	1,184
Financial assets held for sale to NAMA	**77,791**	-	**77,791**	115,008	**-**	115,008
Included elsewhere:						
Accrued interest	**24,324**	-	**24,324**	23,328	-	23,328
	36,691,878	**290,640**	**36,982,518**	39,040,133	268,351	39,308,484
Loan commitments	**190,000**	**-**	**190,000**	443,000	-	443,000
Maximum exposure to credit risk	**36,881,878**	**290,640**	**37,172,518**	39,483,133	268,351	39,751,484

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.

Notes to the accounts

9. Risk management *(continued)*

Credit risk *(continued)*

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

Stress tests undertaken on the Group's credit portfolios form a significant part of the Group's Pillar 1 and Pillar 2 stress tests, as well as stress tests undertaken as part of other regulatory processes.

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. In assessing provisions due account is taken of the impact of negative equity in establishing appropriate provision amounts.

Notes to the accounts

9. Risk management *(continued)*

Credit risk *(continued)*

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.

Individually significant impairment

Each entity within 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.

Notes to the accounts

9. Risk management *(continued)*

Credit risk *(continued)*
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 5 months.

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

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 10).*
- Loans and receivables to banks *(note 11).*
- Loans and receivables to customers *(note 12).*
- Provisions for impairment of loans and receivables *(note 7).*
- Financial assets held for sale to NAMA *(note 16).*

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 Central Bank under a Mortgage-Backed Promissory Note (short term) facility (“**MBPN Facility**”)and other funding from the Central Bank under facilities which may be available to the Bank from time to time;

(d) wholesale and corporate market deposit taking; and

Notes to the accounts

9. Risk management *(continued)*

Funding and Liquidity *(continued)*

(e) capital funding to ensure at a minimum compliance with the capital adequacy requirements of the Central Bank of Ireland.

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 Central Bank of Ireland 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 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. and with the Central Bank of Ireland and access to ECB funding. The table on page 45 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

9. 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.

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.

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.

Notes to the accounts

9. 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 10.

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 2010 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 2010** 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	17,434,889	77,139	599,007	724,880	744,032	190,391	226,980	77,057	-	20,074,375
Loans and receivables to banks	16,470,576	-	-	-	-	-	-	-	-	16,470,576
Derivatives and other financial instruments	-	-	-	-	-	-	-	-	290,640	290,640
Assets classified as held for sale	5,203	-			-	-	-	-	-	-
- 5,203										
Financial assets held for sale to NAMA	77,791	-	-	-	-	-	-	-	-	77,791
Other assets	-	-	-	-	-	-	-	-	63,883	63,883
Total assets	**33,988,509**	**77,139**	**599,007**	**724,880**	**744,032**	**190,391**	**226,980**	**77,057**	**354,523**	**36,982,518**
Liabilities										
Customer accounts	-	-	-	-	-	-	-	-	26	26
Deposits by central banks and banks	27,332,549	-	-	-	-	-	-	-	-	27,332,549
Derivatives and other financial instruments	-	-	-	-	-	-	-	-	3,126	3,126
Debt issued	5,750,000	-	-	-	1,000,000	-	-	1,765,000	292,075	8,807,075
Subordinated liabilities	300,000	-	-	-	-	-	-	-	-	300,000
Other liabilities	-	-	-	-	-	-	-	-	117,104	117,104
Shareholders' funds	-	-	-	-	-	-	-	-	422,638	422,638
Total liabilities	**33,382,549**	**-**	**-**	**-**	**1,000,000**	**-**	**-**	**1,765,000**	**834,969**	**36,982,518**
Derivative financial instruments										
(Interest rate swaps)										
Floating rate interest receivable	20,628,759	-	-	-	-	-	-	-	-	20,628,759
Floating rate interest payable	(17,989,273)	(77,139)	(599,007)	(724,880)	(744,032)	(190,391)	(226,980)	(77,057)	-	(20,628,759)
Floating rate interest payable	(2,765,000)	-	-	-	-	-	-	-	-	(2,765,000)
Fixed rate interest receivable	-	-	-	-	1,000,000	-	-	1,765,000	-	2,765,000
Total derivatives	**(125,514)**	**(77,139)**	**(599,007)**	**(724,880)**	**255,968**	**(190,391)**	**(226,980)**	**1,687,943**	**-**	**-**
Interest sensitivity gap	480,446	-	-	-	-	-	-	-	(480,446)	-
Cumulative interest sensitivity gap	480,446	480,446	480,446	480,446	480,446	480,446	480,446	480,446	-	-

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 central banks and 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	-	

Notes to the accounts

10. 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.

	2010 € 000 Contract/ Notional Amount	**2010 € 000 Fair Value Asset/ (Liability)**	2009 € 000 Contract/ Notional Amount	2009 € 000 Fair Value Asset/ (Liability)
Derivatives classified as trading				
Hedging mortgage loan accounts – outside the Cover Assets Pool	**1,977,244**	**(124)**	4,859,809	(503)
Hedging mortgage loan accounts – within the Cover Assets Pool	**18,651,515**	**(3,002)**	16,073,616	(3,082)
Total derivatives classified as trading	**20,628,759**	**(3,126)**	20,933,425	(3,585)
Derivatives classified as hedging (Debt Securities)				
Interest rate swaps	**2,765,000**	**290,640**	4,740,000	268,351
Total derivatives classified as hedging (Debt Securities)	**2,765,000**	**290,640**	4,740,000	268,351
Total derivatives	**23,393,759**	**287,514**	25,673,425	264,766

The following table represents the underlying principal and gross replacement costs of the Bank's derivatives as at 31 December 2010.

	Residual Maturity 2010				Residual Maturity 2009			
31 December 2010	**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	**20,628,759**	**1,000,000**	**1,765,000**	**23,393,759**	22,933,425	1,000,000	1,740,000	25,673,425
Gross replacement costs								
Interest rate contracts	**-**	**79,293**	**280,060**	**359,353**	74,239	79,813	251,320	405,372

Notes to the accounts

10. 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 2010.

	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					-
1-5 years					54,019
Over 5 years					236,621
	2,765,000	**5.16**	**4.48**		**290,640**
Pay floating					
1 year or less					
1-5 years					
Over 5 years					
	2,765,000	**0.08**		**0.93**	**0**
Other Interest rate derivatives*					
Interest rate swaps:					
Pay floating					
1 year or less					
1-5 years					(46,096)
Over 5 years					
	20,628,759	**0.08**		**2.64**	**(46,096)**
Receive floating					
1 year or less					42,970
1-5 years					
Over 5 years					
	20,628,759	**0.08**	**2.45**		**42,970**

* 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

10. 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 2010.

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

	2010 Carrying Amount € 000	**2010 Fair value Amount € 000**	2009 Carrying Amount € 000	2009 Fair Value Amount € 000
Assets				
Cash and balances at central bank	**50**	**50**	50	50
Derivative financial instruments	**290,640**	**290,640**	268,351	268,351
Loans and receivables to banks	**16,470,576**	**16,470,576**	18,208,051	18,208,051
Loans and receivables to customers	**20,074,375**	**17,986,640**	20,692,512	20,734,512
Assets classified as held for sale	**5,203**	**5,203**	1,184	1,184
Financial assets held for sale to NAMA	**77,791**	**31,116**	115,008	115,008
Liabilities				
Deposits by central banks and banks	**27,332,549**	**27,332,549**	27,474,129	27,474,129
Customer accounts	**26**	**26**	175	175
Derivative financial instruments	**3,126**	**3,126**	3,585	3,585
Debt securities in issue	**8,807,075**	**7,574,728**	10,760,078	10,447,658
Subordinated liabilities	**300,000**	**69,530**	300,000	171,000

Notes to the accounts

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

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

Loans and receivable to banks

The fair value of loans and receivables to banks are estimated using discounted cash flows applying either market rates, where practicable, or rates currently offered by other financial institutions for placings with similar characteristics

Financial assets held for sale to NAMA

The financial assets held for sale to NAMA are measured on the same basis in the statement of financial position as prior to their classification as held for sale. At 31 December 2010, it was deemed unavoidable that the remaining NAMA assets would transfer at a discount of approximately 60% of their gross carrying value. Accordingly, it is considered appropriate to use this discount in determining the fair value for the remaining NAMA assets. The financial assets held for sale to NAMA at 31 December 2010 were transferred to NAMA in March 2011.

Loans and receivables to customers

The Bank provides lending facilities of varying rates and maturities to personal customers. Valuation techniques are used in estimating the fair value of loans, primarily using discounted cash flows, applying market rates where practicable. The fair value of fixed rate loans is calculated by discounting expected cash flows using discount rates that reflect the credit and interest rate risk in the portfolio. In addition to the assumptions set out under the valuation technique, regarding cash flows and discount rates, a key assumption for the loans and receivables is that the carrying value of variable rate loans approximates to market value where there was no significant change in the credit risk of the borrower. In deriving a fair value, the adjustment for credit risk took into account the forecast provisions and losses for the period 2011-2013.

In preparing the 2010 AIB Group accounts, the fair value of customer loans is calculated based on an average of the PCAR Base and Stressed scenarios covering provisioning and delevaraging assumptions.

In preparing the 2010 AIB Mortgage Bank accounts consideration was given to the impact of future funding costs and potential deleverage scenarios on the fair value of customer loans. Given the inherent uncertainties in these future scenarios, the same methodology as applied in the AIB Group Accounts has been applied in calculating the Bank's fair value of customer loans.

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 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.

Subordinated liabilities

The fair value of the subordinated liabilities was estimated using quoted market prices where available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar instruments. 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.

Notes to the accounts

11. Loans and receivables to banks	2010 € 000	2009 € 000
Funds placed with Allied Irish Banks, p.l.c.		
Analysed by remaining maturity:		
- 3 months or less	**10,255,559**	9,718,051
- 1 year or less but over 3 months	**-**	-
- 5 years or less but over 1 year	**4,250,000**	6,750,000
- Greater than 5 years	**1,765,000**	1,740,000
Funds placed with Barclays Bank, p.l.c.		
Analysed by remaining maturity:		
- 3 months or less	**200,017**	**-**
	16,470,576	18,208,051

The balances with Allied Irish Banks, p.l.c. include a balance of €519m held as collateral for the derivatives noted in note 10. The balances held with Barclays Bank, p.l.c. represent the Cash Substitution Pool Assets.

12. Loans and receivables to customers	2010 € 000	2009 € 000
Analysed by remaining maturity:		
- Repayable on demand	**839,510**	381,740
- 3 months or less	**10,448**	13,818
- 1 year or less but over 3 months	**82,510**	54,802
- 5 years or less but over 1 year	**397,833**	453,382
- Greater than 5 years	**19,185,549**	19,904,980
Provisions for impairment of loans and receivables (note 7)	**(441,475)**	(116,210)
	20,074,375	20,692,512

The method for analysing the remaining maturity was amended in 2010 to more accurately reflect the underlying loan terms. 2009 balances have been represented on a consistent basis.

The unwind of the discount on the impairment provision amounted to €4.6m (2009: €1.9m) 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.

Notes to the accounts

12. Loans and receivables to customers *(continued)*

By geographic location and sector	**2010** **€ 000**	2009 € 000
Republic of Ireland		
Home mortgages (net of provisions)	**20,074,375**	20,692,512
	20,074,375	20,692,512

13. Additional information on credit risk

Aged analysis of contractually past due but not impaired facilities – 31 December 2010

	1-30days € 000	**31-60days € 000**	**61-90days € 000**	**91+days € 000**	**Total € 000**
Home mortgages	**377,700**	**180,250**	**116,180**	**253,000**	**927,130**
	377,700	**180,250**	**116,180**	**253,000**	**927,130**
As a percentage of total loans	**1.8%**	**0.9%**	**0.6%**	**1.2%**	**4.5%**

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
As a percentage of total loans	1.1%	0.5%	0.3%	0.4%	2.7%

As at 31 December 2010, there were no mortgage loan accounts (Nil in 2009) 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 19(c).

Total loans relate to loans and receivables to customers and are gross of provisions and unearned income.

Notes to the accounts

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

Individually impaired loans by geographic location and sector

	2010	2009
	€ 000	€ 000
Republic of Ireland		
Home mortgages	**839,510**	381,740
	839,510	381,740

Provision cover table

	Impaired loan Balance	**Specific Provision**	**Specific Provision Cover %**
Republic of Ireland			
Home mortgages – 31 December 2010	839,510	160,568	19%
Home mortgages – 31 December 2009	381,740	67,703	18%

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.

14. Other assets	**2010** **€ 000**	2009 € 000
Accrued interest	**24,324**	22,645
Other assets	**-**	683
	24,324	23,328

Notes to the accounts

15. Deferred taxation	**2010 € 000**	2009 € 000
At 1 January 2010	**-**	-
Unutilised tax losses	**39,559**	-
At 31 December 2010	**39,559**	**-**

Deferred tax assets relating to unutilised tax losses and deductible temporary differences are recognised if it is probable that they can be offset against future taxable profits and their utilisation is dependant on future taxable profits.

The Directors have considered the assumptions underpinning the Mortgage Bank plans and have determined that future taxable profits will be available to absorb the deferred tax assets including the unutilised tax losses. Accordingly, it is considered that recoverability of the deferred tax asset is probable.

16. 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 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.

Allied Irish Banks, p.l.c. and each of its subsidiaries, were designated a participating institution under the Act on 12 February 2010. BZWBK and its subsidiaries were excluded from this designation. For AIB Mortgage Bank at 31 December 2010, €214m of assets had transferred to NAMA, leaving a residual of €78m which is due to transfer early in 2011.
The financial assets held for sale to NAMA at 31 December 2010 were transferred to NAMA in March 2011.

The consideration for the NAMA assets acquired from AIB Mortgage Bank comprises the issue to AIB of NAMA bonds and subordinated NAMA bonds equal in nominal value to the purchase price of the NAMA Assets. However, the fair value of such bonds has differed to the nominal value, depending upon the terms of issue.

The following table provides an analysis of assets classified as held for sale to NAMA.

	2010 € 000	2009 € 000
Loans and receivables held for sale to NAMA	**77,711**	114,846
Accrued income on assets held for sale to NAMA	**80**	162
	77,791	115,008

Notes to the accounts

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

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

	2010	2009
	€ 000	€ 000
Republic of Ireland		
Home Mortgages (net of provisions)	**77,791**	115,008
	77,791	115,008

Aged analysis of contractually past due but not impaired facilities held for sale to NAMA – 31 December 2010

	1-30days	**31-60days**	**61-90days**	**91+days**	**Total**
	€ 000	**€ 000**	**€ 000**	**€ 000**	**€ 000**
Republic of Ireland					
Home mortgages	**1,986**	**651**	**715**	**3,828**	**7,180**
	1,986	**651**	**715**	**3,828**	**7,180**
As a percentage of total loans held for sale	**2.6%**	**0.8%**	**0.9%**	**4.9%**	**9.2%**

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

	1-30days	**31-60days**	**61-90days**	**91+days**	**Total**
	€ 000	**€ 000**	**€ 000**	**€ 000**	**€ 000**
Republic of Ireland					
Home mortgages	2,960	1,490	150	1,590	6,190
	2,960	1,490	150	1,590	6,190
As a percentage of total loans held for sale	2.6%	1.3%	0.1%	1.4%	5.4%

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

	2009	2009
	€ 000	€ 000
Republic of Ireland		
Home mortgages	**37,290**	10,321
	37,290	10,321

Notes to the accounts

17. Assets classified as held for sale

At 31 December 2010, 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 €5.2m 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.

18. Deposits by central banks and banks	**2010** **€ 000**	2009 € 000
Due to Allied Irish Banks, p.l.c.	**24,582,549**	25,974,129
Due to Central Bank*	**2,750,000**	1,500,000
	27,332,549	27,474,129

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 2010, the amount due to the Central Bank comprised €1.85bn (2009: €1.5bn) in respect of mortgage covered securities repoed with the ECB and €0.9bn (2009: Nil) under the Mortgage-Backed Promissory Note facility available outside of normal ECB open market operations.

At 31 December 2010, of the €6.2bn mortgaged covered securities issued to AIB Mortgage Bank, €2.5bn was used to provide €1.85bn liquidity under a sale and repurchase agreement by AIB Mortgage Bank with the ECB with a maturity date in January 2011. The remaining €3.7bn of mortgage covered securities issued to AIB Mortgage Bank was repoed at nil value with Allied Irish Banks, p.l.c. and was then subject to a sale and repurchase agreement with the ECB, providing liquidity for AIB Group of €2.5bn.

The AIB Mortgage Bank Mortgage-Backed Promissory Note facility with the Central Bank was used as a source of liquidity during the year with a maximum drawdown of €1.5bn. As from 20 December 2010, the facility, for normal ECB open market operations, was no longer available due to a ratings downgrade by Moody's of Allied Irish Banks, p.l.c.. Accordingly, Nil was drawdown as at 31 December 2010 (31 December 2009: Nil drawdown). The AIB Mortgage Bank Mortgage-Backed Promissory Note Framework has been used as a source of liquidity with the Central Bank of Ireland outside of normal ECB open market operations since November 2010; as at 31 December 2010, €0.9bn was drawn down (2009: Nil drawdown).

19. Debt securities in issue	**2010** **€ 000**	2009 € 000
Mortgage covered securities in issue to external investors of €3.1bn (2009: €5.0bn) and in issue to Allied Irish Banks, p.l.c. of €5.75bn (2009: €5.75bn) by remaining maturity:		
- 1 year or less	**2,500,000**	2,005,257
- 5 years or less but over 1 year	**4,304,216**	6,804,806
- Greater than 5 years	**2,002,859**	1,950,015
	8,807,075	10,760,078

Notes to the accounts

19. Debt securities in issue *(continued)*	**2010 € 000**	2009 € 000
Mortgage covered securities in issue to external investors and internal issuances at nominal value:		
- External investors	**2,765,000**	4,740,000
- Allied Irish Banks, p.l.c.	**5,750,000**	5,750,000
- AIB Mortgage Bank	**6,150,000**	3,500,000
	14,665,000	13,990,000

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 by AIB Mortgage Bank, the transaction gives rise to the recognition of an asset and a liability. (See note18).

Mortgage covered securities issued to Allied Irish Banks, p.l.c. were subject to sale and repurchase agreements with the ECB at 31 December 2010, providing liquidity for AIB Group of €5.2bn.

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 2010, the Cover Assets Pool amounted to €18.9bn (€19.6bn in 2009), comprising of €18.7bn (€16.1bn in 2009) of mortgage credit assets (mortgage loan accounts) and €0.2bn (€3.5bn in 2009) of substitution assets (cash on deposit with Barclays Bank, p.l.c. (2010) and (2009) 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.

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

From	**To**	**Total Loan Balances (1 & 2) 2010 € m**	**Number of Mortgaged Properties 2010**	Total Loan Balances (1 & 2) 2009 € m	Number of Mortgaged Properties 2009
0	€100,000	**1,918**	**37,357**	1,858	36,450
€100,000	€200,000	**5,360**	**36,260**	4,553	31,038
€200,000	€500,000	**8,537**	**29,904**	7,393	25,746
Over €500,000		**2,837**	**3,369**	2,270	2,834
		18,652	**106,890**	16,074	96,068

(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 124,871 loan accounts (112,121 in 2009) secured on 106,890 properties (96,068 in 2009).

Notes to the accounts

19. Debt securities in issue *(continued)*

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

Geographical Area	Number of Mortgaged Properties 2010		Number of Mortgaged Properties 2009	
Co. Dublin	**23,188**	**22%**	20,454	21%
Outside Dublin	**83,702**	**78%**	75,614	79%
	106,890	**100%**	96,068	100%

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

As at 31 December 2010, there were no mortgage loan accounts (Nil in 2009) in default in the Cover Assets Pool (in default being defined as mortgage loan accounts in arrears by three months or more).

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

During the year ended 31 December 2010, 4 mortgage loan accounts (6 in 2009) in the Cover Assets Pool had been in default with arrears greater than €1,000. As at 31 December 2010, there were no accounts in default in the Cover Assets Pool (Nil in 2009). The basis on which this year's and last year's comparative numbers were calculated has been amended to more accurately identify loans in default.

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

During the year ended 31 December 2010, 87 non-performing mortgage loan accounts (7 in 2009) 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. The basis on which this year's and last year's comparative numbers were calculated has been amended to more accurately identify loans in default.

19 (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 1,241 accounts (503 in 2009) as at 31 December 2010 was €1,044,997 (€614,259 in 2009). None of the accounts in question were written off as at 31 December 2010, as they were in arrears by less than three months.

19 (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 2010 was €1,542m (€1,393m in 2009), of which €1,127m (€998m in 2009) represented repayment of principal and €415m (€395m in 2009) 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.

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

As at 31 December 2010 there were no loan accounts (Nil in 2009) in the Cover Assets Pool that were secured on commercial properties.

Notes to the accounts

20. Accruals and deferred income	2010 € 000	2009 € 000
Interest payable on mortgage covered securities	**68,819**	137,014
Expenses	**3,477**	1,928
	72,296	138,942

21. Subordinated liabilities	2010 € 000	2009 € 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.

(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.

Notes to the accounts

22. Provisions for liabilities and commitments	**2010 € 000**	2009 € 000
Provision for loss on transfer of loans to NAMA	**43,905**	-
Other provisions	**523**	-
	44,428	-

At 31 December 2010, the transfer of certain loans to NAMA was deemed unavoidable, accordingly a provision of €43.9m, being a constructive obligation, has been made for the expected discount determined to be 60 per cent on a gross carrying value of loans amounting to €77.8m which are expected to transfer to NAMA early in 2011.
Other provisions of €0.5m (2009: Nil) relates to a provision to cover repayment of surcharge interest to customers.

23. Share capital	**2010 € 000**	2009 € 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		
(2009: 450,000,000 ordinary shares of €1.00 each)	**450,000**	450,000
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.

24. Capital reserves	**2010 € 000**	2009 € 000
Capital reserves	**80,000**	-
	80,000	-

The Bank received a capital contribution of €80m from its parent Allied Irish Banks, p.l.c. as a result of the capital deficit arising from the loan provisions recorded in the financial statements to 31 December 2010

Notes to the accounts

25. 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.

Capital resources and regulatory capital ratios
The table below shows AIB Mortgage Bank's capital resources as at 31 December 2010 and 31 December 2009.

	Basel II	Basel II
	2010	2009
	€'000	€'000
Shareholders' equity	**422,638**	619,550
Dated capital notes	**100,000**	100,000
Undated capital notes	**200,000**	200,000
Total capital resources	**722,638**	919,550

Capital resources decreased by €196.9m during the year ended 31 December 2010. This decrease arose as a result of net loss in the accounts, offset by a capital contribution from AIB.

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.

	2010	2009
26. Dividend	**€ 000**	€ 000
Dividend Paid	-	-

No dividend has been recommended for approval, payable to the Bank's parent company, Allied Irish Banks, p.l.c. at 31 December 2010.

Notes to the accounts

27. Employee Information

For the year ended 31 December 2010 the average number of employees was 6 (2009: 6). As at 31 December 2010, the Bank had 6 employees.

28. Statement of cash flows	2010 € 000	2009 € 000
Loans and receivables to Allied Irish Banks, p.l.c.	**839,887**	840,138
Cash and cash equivalents	**839,887**	840,138

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

29. Auditor's fees	2010 € 000	2009 € 000

The disclosure of Auditor's fees have been reclassified in 2010 in accordance with (SI220)[1] which mandates fees in particular categories and that fees paid to the AIB Mortgage Bank's Auditor (KPMG Ireland) for services to the Bank only be disclosed in this format. Comparatives have been restated on a basis consistent with 2010 as detailed in the table below.

Auditor's fees (excluding vat)		
Audit	**55**	55
Other assurance services	**-**	11
Total auditor's fees	**55**	66

Other assurance services include fees for additional assurance issued by the firm outside of the audit of the statutory financial statements.

[1] SI220 is titled the European Communities (Statutory Audits) (Directive 2006/43/EC) Regulations 2010.

30. Directors' remuneration	2010 € 000	2009 € 000
Fees	**31**	42
	31	42

31. Reporting currency

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

Notes to the accounts

32. Segmental Information

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

33. Contingent liabilities and commitments

Contingent Asset/Liability-NAMA

On 17 December 2010, part of the final tranche of loans with a net carrying value of €167m was transferred to NAMA. An aggregate discount of 60 per cent. was applied to the gross carrying value of the loans. This transfer was not subject to due diligence at that time but will take place in 2011 which will set the final haircut for this transfer. However, it is not expected that the final discount will differ materially from the 60 per cent.

Under NAMA legislation, an institution can formally raise an objection to the portfolio acquisition value specified in the acquisition schedule. As the timing of any formal objection is unknown at this time but is not expected to be completed until 2012, this may result in an inflow of economic benefit to the Group.

In addition, AIB provided for a constructive obligation in respect of loans due to transfer to NAMA in 2011.The discount applied to the expected transfer was 60 per cent based on previous experience and statements from the Irish Minister for Finance. If the discount ultimately proves to be lower/higher than the 60 per cent. provided, an inflow/outflow of economic benefits may result to AIB.

At 31 December 2010 the Bank had €190m (2009: €443m) of approved mortgage loan applications that had not been drawn down as at the year end.

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

Since the commencement of the financial crisis in 2008, the Irish Government has taken a range of measures to stabilise the Irish banking system. This has culminated in the passing into law on 21 December 2010 of the Credit Institutions (Stabilisation) Act 2010 and the subsequent issue by the High Court of a Director Order to AIB. Additionally, on 31 March 2011, following completion of PCAR and PLAR assessments which took place in February/March 2011, the Central Bank published the Financial Measures which details the outcome of its review of the capital and funding requirements of the domestic Irish Banks. At the same time, the Department of Finance announced a restructuring of the Irish Banking system. Details of these events are set out on note 34 'Non adjusting events after the reporting period'.

Prior to this, other measures introduced by the Irish Government 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");
(v) Facility with the Central Bank of Ireland; and
(vi) Joint EU-IMF Programme for Ireland.

The rights and powers given to the Minister for Finance ('the Minister') and/or the Central Bank under the Credit Institutions (Stabilisation) Act 2010 and the High Court Direction Order are set out below. In addition, other rights and powers given to the Minister and/or the Central Bank over the operations of AIB Group (and other financial institutions) arising from the various stabilisation measures include:
(a) 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 is prohibited;
(b) certain dated subordinated debt covered by the guarantee, including the maintenance of solvency ratios during the guarantee period;

Notes to the accounts

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

(c) 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;
(d) the appointment of non-executive directors to its board (three such directors have been nominated by the Minister and appointed to the Board);
(e) changes to the Board where the Board does not contain an appropriate balance between executive and non-executive directors;
(f) the appointment of persons to attend all meetings of the remuneration, audit, credit and risk committees of AIB;
(g) restructure its executive management responsibilities, strengthen its management capacity and improve its corporate governance;
(h) declaration and payment of dividends;
(i) restrictions in relation to directors' and executives' remuneration and termination payments;
(j) buy-backs or redemptions of its shares;
(k) 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
(l) restrictions over the manner in which AIB can deal with its NAMA assets.

The Central Bank in consultation with the Minister, may 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 Central Bank, following consultation with the Minister, may direct.

AIB must comply with targets set for AIB by the Central Bank, 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. The 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.

Measures of support received from the Irish Government are set out in (i) to (vi) below. These Irish Government measures and the ability of the European Commission to influence the future composition of the Group's businesses are significant factors that may influence our future results and financial condition.

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

The Act provides broad powers to the Minister (in consultation with the Governor of the Central Bank of Ireland) to act on financial stability grounds to effect the restructuring actions and recapitalisation measures envisaged in the Programme.

The Act applies to banks who have received financial support from the State, building societies and credit unions. Given the exceptional nature of the powers contained in the Act, the powers are time-limited and scheduled to expire on 31 December 2012. The powers provided in the Act allow the Minister to implement key aspects of the agreed Programme for bank restructuring as follows:

- issue directions to take or prevent any actions in order to support the Government's banking strategy;
- transfer relevant institutions' assets and liabilities to facilitate the restructuring of the banking sector; and
- make subordinated liabilities orders, on a case by case basis and under particular conditions, to achieve appropriate burden sharing by subordinated creditors in relevant institutions which have received State support.

Notes to the accounts

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

Following the implementation of the Act, the Irish Government applied to the High Court on 23 December 2010 for a Direction Order under the Act, which it received. The Direction Order directed AIB to increase its authorised share capital and to adopt amended Articles of Association to give effect to the capital increase and to issue to the National Pension Reserve Fund Commission ("NPRFC"):

(i) 675,107,845 ordinary shares of €0.32 each at an issue price per share of €0.3793; and

(ii) 10,489,899,564 convertible non-voting shares of €0.32 each (the "CNV Shares") at an issue price per share of €0.3396.

This resulted in gross proceeds of €3,818.4 billion before costs of €65.9 million and a fee amounting to €52.5 million for cancellation of outstanding warrants held by the NPRFC under the 2009 recapitalisation.

The CNV shares rank equally with the ordinary shares, other than in respect of voting, and will be convertible into ordinary shares on a one-for-one basis at any time at the election of the holder. The CNV Shares have no voting rights until the completion of the BZWBK disposal, and thereafter the voting rights of the CNV Shares will be confined to resolutions that propose to vary or abrogate their rights or propose to wind up AIB. The NPRFC subscribed for CNV Shares instead of ordinary shares to ensure the holding of ordinary shares did not exceed 49.9% of the issued ordinary shares pending the completion of the BZWBK disposal. Following completion of the Polish disposal, the NPRFC converted its holding in AIB's CNV shares into ordinary shares on 8 April 2011. As a result of these actions the State holds 92.8% of the ordinary share capital of AIB. Prior to the conversion of the CNV Shares, this amounted to 49.9%.

The High Court also directed AIB to apply to cancel its listing of ordinary shares on the Main Securities Market and to apply for listing on the Enterprise Securities Market ("ESM") of the Irish Stock Exchange. This is to ensure that shareholders retain access to a public trading facility for their shares. Shareholders' ownership of, and rights over, the existing ordinary shares will be unaffected by this move.

The High Court further directed AIB to cancel the admission of its ordinary shares to the Official List maintained by the UK Financial Services Authority and to cancel trading on the main market of the London Stock Exchange.

The High Court also directed AIB to complete the sale of its Polish interests to Banco Santander. The sale completed on 1 April 2011.

The Irish Government, by virtue of the High Court Direction Order to AIB under the Credit Institutions (Stabilisation) Act 2010, the guarantee schemes detailed below and the issue to the NPRFC of the €3.5 billion preference shares is related to AIB.

Other measures of support received from the Irish Government:

(i) The Credit Institutions (Financial Support) Scheme 2008

The CIFS Scheme, which expired on 29 September 2010, gave effect to the bank guarantee announced by the Irish Government on 30 September 2008. Under the CIFS Scheme, the Minister for Finance guaranteed certain types of liabilities of certain participating institutions, including AIB and certain of its subsidiaries, for a two-year period from 30 September 2008.

From the time that a participating institution joins the ELG Scheme, as outlined below, 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. From the time a participating institution joins the ELG Scheme, any liabilities incurred or contracted for thereafter by that participating institution may be guaranteed under the ELG Scheme only.

Notes to the accounts

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

(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 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 minister stands as guarantor of all guaranteed liabilities of a participating institution.

The ELG Scheme is intended to facilitate the ability of credit institutions in Ireland to issue certain debt securities and take deposits with a maturity of up to five years on debt securities issued or deposits taken between the period 21 January 2010 and 30 June 2011. The original date for periods covered for taking deposits and issuing securities was set at 29 September 2010, however, that extended to 31 December 2010 and further extended to 30 June 2011 following approval by the European Commission.

Each AIB ELG participating institution agreed to be bound by the terms of the ELG Scheme and to indemnify the Minister against all payments which the Minister may be required to make under the ELG Scheme in respect of liabilities of the AIB ELG participating institutions.
Eligible liabilities under the ELG Scheme comprise the following liabilities:

- all deposits (to the extent not covered by deposit protection schemes in Ireland or in any other jurisdiction);
- senior unsecured certificates of deposit;
- senior unsecured commercial paper;
- other senior unsecured bonds and notes; and
- other forms of senior unsecured debt which may be specified by the Minister consistent with European Union state aid rules and the European Commission's Banking Communication (2008/C 270/02) and subject to prior consultation with the European Commission, incurred by a participating institution during the period from the date it joined the ELG Scheme (i.e. 21 January 2010 in the case of AIB ELG participating institutions) up to 30 June 2011.

An eligible liability must not have a maturity in excess of five years and must be incurred during an 'issuance window' which is the period during which a guaranteed deposit can be made or guaranteed debt issued. The next review of the ELG Scheme by the European Commission is due to take place before 30 June 2011 although the result of any such review will not affect the status of guaranteed liabilities that are, by then, already in place. Accordingly, the 'issuance window' in respect of every eligible liability of a participating institution under the ELG Scheme (including retail deposits over €100,000 for any duration up to five years and corporate and inter-bank deposits for any duration up to five years) has been extended from 31 December 2010 to 30 June 2011 so that a State guarantee is available for short and long-term liabilities issued or accepted up to 30 June 2011. Retail deposits of an amount up to €100,000 remain outside the ELG Scheme but continue to be guaranteed indefinitely under the Deposit Guarantee Scheme.

The ELG Scheme is not a blanket guarantee. Under the terms of the ELG Scheme, a participating institution must apply to the Minister for an eligible liability or eligible liabilities issued under a programme to be guaranteed under the ELG Scheme and those eligible liabilities will only be guaranteed if the NTMA, with delegated authority from the Minister, accepts an application from a participating institution for the inclusion of the eligible liability or those eligible liabilities in the ELG Scheme.

Notes to the accounts

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

From the time that a participating institution is designated as such under the ELG Scheme, any liabilities incurred or contracted for thereafter by that participating institution may be guaranteed under the ELG Scheme only if not already covered under the existing Deposit Guarantee Scheme. However, dated subordinated debt and asset-covered securities issued after a covered institution joined the ELG Scheme are not guaranteed under the ELG Scheme.

Participating institutions must pay a fee to the Minister in respect of each liability guaranteed under the ELG Scheme. Participating institutions will also be required to indemnify the Minister for any costs and expenses of the Minister and for any payments made by the Minister under the ELG Scheme which relate to the participating institution's guarantee under the ELG Scheme.

Details of amounts paid/allocated to AIB Mortgage Bank are set out in note 2 and 4.

(iv)Participation in the National Asset Management Agency ("NAMA")
On 7 April 2009, the Minister announced the Government's intention to establish the National Asset Management Agency. On 22 November 2009, the NAMA Act was enacted providing for the establishment of the National Asset Management Agency. 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. BZWBK and its subsidiaries were excluded from the designation.

AIB commenced the transfer process to NAMA in April 2010. The consideration for the NAMA assets acquired from AIB comprised the issue to AIB of NAMA bonds and subordinated NAMA bonds. By 31 December 2010, AIB had transferred €18.6 billion of assets to NAMA in return for the issue to it of €8.5 billion of NAMA bonds (including subordinated bonds), which represented a discount of approximately 54.5 per cent to the gross carrying value of the assets transferred.

In relation to these transferred assets, AIB will continue to service them on behalf of NAMA in return for a service fee. (As at 31 December 2010, approximately €2.3 billion gross of AIB's assets remain to be transferred to NAMA under the NAMA Act. AIB expects that those residual assets will be transferred to NAMA by 31 March 2011).

On 28 November 2010, the Irish Government announced that, with regard to AIB, the previous minimum threshold of €20 million for NAMA Assets to transfer to NAMA would be removed. On 26 January 2011, the Minister introduced the NAMA (Amendment) Bill (the 'Bill') in the Oireachtas (the Irish Parliament) to give effect to this change to the NAMA Programme. This Bill has yet to be passed into law.

(v) Funding from the Central Bank of Ireland
Arising from the difficulties encountered by AIB (and other financial institutions) in sourcing funding during the latter half of 2010, the Central Bank of Ireland entered into a number of agreements with AIB in addition to the agreements already in place with both AIB and AIB Mortgage Bank. See note 33 Related party transactions for amounts drawn down from the Central Bank at 31 December 2010.These agreements are detailed below.

Mortgage Backed Promissory Notes – Allied Irish Banks, p.l.c.
Allied Irish Banks, p.l.c. ("AIB") and the Central Bank entered into a Framework agreement in respect of the issue of Mortgage Backed Promissory Notes ("MBPN"). Under the terms of this agreement, the Central Bank may advance funds to AIB on foot of one or more MBPNs issued by AIB.

Notes to the accounts

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

Master Loan Repurchase Deed
AIB and the Central Bank have entered into a Master Loan Repurchase Deed. Under this agreement, AIB agreed to sell to the Central Bank certain loans together with their related security with a simultaneous agreement by the Central Bank to sell to AIB equivalent loan assets on a certain future date.

Mortgage Backed Promissory Notes – AIB Mortgage Bank
AIB Mortgage Bank ("AIBMB") entered into a framework agreement with the Central Bank in respect of the issue of Mortgage Backed Promissory Notes. Under the terms of this agreement, obligations are secured by way of a first floating charge to the Central Bank over all its right title, interest and benefit, in loans and receivable to customers.

Other funding from the Central Bank of Ireland
The Group also has funding from the Central Bank through ECB Monetary Policy Operation Sale and Repurchase Agreements. This funding amounted to €25.2bn at 31 December 2010. These agreements were for maturities of between 7 days and 3 months, with a current interest rate of 1% in all cases. These facilities mature on dates between 5 January and 31 March 2011.

Facility Deed Agreement with the Central Bank of Ireland
Under this agreement, the Central Bank may make loans to AIB which are guaranteed by the Minister. AIB in turn, has agreed to indemnify the Minister against any payment the Minister makes in relation to the guarantee. This agreement is next due for renewal in May 2011.

(vi) Joint EU-IMF Programme for Ireland
On 28 November 2010, the Irish Government agreed in principle to the provision of €85 billion of financial support to Ireland through the European Union ("EU") and the International Monetary Fund ("IMF"). The Irish Government will contribute €17.5bn from the NPRFC and other domestic cash resources. This means that the extent of external assistance will be reduced to €67.5bn.

The purpose of the external financial support is to return the economy to sustainable growth and to ensure a properly functioning healthy banking system. Up to €35 billion of the support is earmarked for the banking system, €10 billion for immediate recapitalisation and the remaining €25 billion will be provided on a contingency basis.

The programme of support by the EU and IMF has two parts – the first part deals with bank restructuring and reorganisation and the second part deals with fiscal policy and structural reform.

The programme for the recovery of the banking system will be an intensification of the measures already adopted by the Government. The programme provides for a recapitalisation, fundamental downsizing, restructuring and reorganisation of the banking sector. The outcome will lead to a smaller banking system more proportionate to the size of the economy, capitalised to the highest international standards, with renewed access to normal market sources of funding and focused on strongly supporting the recovery of the economy. The main elements of the programme impacting on AIB are as follows:

- Additional capital requirements have been set which build on the results of the Central Bank's Prudential Capital Assessment Review ("PCAR") carried out earlier in 2010.
- Immediate recapitalisation of the domestic banking system raising Core Tier 1 capital ratios to at least 12%. Along with early measures to support deleveraging set out below, this will result in an immediate injection of €10 billion of fresh capital into the banking system, above and beyond that already committed.
- Further recapitalisation to take place in the first half of 2011 as necessary, based on the results of a detailed review and updating of the banks' capital needs following a revised PCAR exercise undertaken by the Central Bank and involving stringent stress testing.

Notes to the accounts

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

- A Prudential Liquidity Assessment Review ("PLAR") to be implemented by the Central Bank for the domestic banks to identify deleveraging actions necessary to significantly reduce their reliance on short term funding.
- A substantial downsizing of the banking system to be achieved through early and decisive actions including:
  - Banks to be required to run down non-core assets, securitise and/or sell portfolios or divisions with credit enhancement provided by the State, if needed.
  - The NAMA Scheme to be extended to remove remaining vulnerable land and development loans from the two largest domestic banks, AIB and Bank of Ireland by end of quarter one, 2011.
  - Banks to be required to promptly and fully provide for all non-performing 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 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..

35. 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. Interest paid to AIB and interest received from AIB are disclosed in Note 1 and Note 2 to the accounts. As at 31 December 2010, 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..

(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.

Notes to the accounts

35. Related party transactions *(continued)*

(b) Transactions with key management personnel (continued)

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 2009 €'000	Amounts advanced during 2010 €'000	Amounts repaid during 2010 €'000	Balance at 31 December 2010 €'000
Kieran Crowley				
Loans	1,089	-	-	1,089
Interest charged during 2010	-	-	-	22
Maximum debit balance during 2010	-	-	-	1,089
Michael Keegan				
Loans	406	-	9	397
Interest charged during 2010	-	-	-	8
Maximum debit balance during 2010	-	-	-	406
David Kelly				
Loans	596	-	13	583
Interest charged during 2010	-	-	-	11
Maximum debit balance during 2010	-	-	-	596
Jennifer Winter				
Loans	92	-	11	81
Interest charged during 2010	-	-	-	2
Maximum debit balance during 2010	-	-	-	92

No other Directors in office during 2010 had loan facilities with AIB Mortgage Bank. .

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.

	2010 **€ 000**	2009 € 000
Aggregate loan amounts outstanding at year end		
Directors	2,150	2,183

Notes to the accounts

35. Related party transactions *(continued)*

(c) Connected Persons

The aggregate of loans to connected persons of directors in office as at 31 December 2010, as defined in Section 26 of the Companies Act 1990, pursuant to a notification received from the Central Bank of Ireland under Section 10 of the Central Bank Act 1971, are as follows:

	Balance at 31 December 2009	**Amounts advanced during 2010**	**Amounts repaid during 2010**	**Balance at 31 December 2010**
	€'000	**€'000**	**€'000**	**€'000**
(Aggregate of 1 person)				
Loans	375	-	9	366
Interest charged during 2010	-	-	-	6
Maximum debit balance during 2010	-	-	-	375

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.

(d) Funding support

At 31 December 2010, of the €6.2bn mortgaged covered securities issued to AIB Mortgage Bank, €2.5bn was used to provide €1.85bn liquidity under a sale and repurchase agreement by AIB Mortgage Bank with the ECB with a maturity date in January 2011. The AIB Mortgage Bank Mortgage-Backed Promissory Note Framework has also been used as a source of liquidity with the Central Bank of Ireland outside of normal ECB open market operations since November 2010; as at 31 December 2010, €0.9bn was drawn down (2009: Nil drawdown).

36. Non adjusting events after the reporting period

The following are the significant non-adjusting events that have taken place since 31 December 2010.

Transfer of mortgage intermediary originated business into AIB Mortgage Bank
On 25 February 2011, Allied Irish Banks, p.l.c. transferred substantially all of its mortgage intermediary originated Irish residential loans, related security and related business to AIB Mortgage Bank. The aggregate principal amount outstanding of and accrued but unpaid interest on, the Irish residential loans transferred by Allied Irish Banks, p.l.c. to AIB Mortgage Bank on 25 February 2011 was approximately €4.2 billion. The transfer was affected pursuant to the statutory transfer mechanism provided for in the Asset Covered Securities Acts.

Transfer of loans to NAMA
On 4 March 2011, AIB transferred a tranche of loans and receivables to NAMA which were included in 'financial assets held for sale to NAMA' in the statement of financial position at 31 December 2010.The carrying value net of provisions of the assets transferred amounted to €0.8 billion, with the proceeds on sale amounting to €0.4 billion giving rise to a loss on disposal of €0.4 billion. This loss had been fully provided for at 31 December 2010.

Notes to the accounts

36. Non adjusting events after the reporting period *(continued)*

Financial Measures Programme/Government restructuring of Irish domestic banks
On 31 March 2011, the Central Bank published the Financial Measures Programme Report which details the outcome of its review of the capital (PCAR) and funding (PLAR) requirements of domestic Irish banks. The main features of this report as impacting on AIB are as follows:
- a minimum capital target of 10.5% core tier 1 in the base scenario, and a 6% core tier 1 in the stress scenario, plus an additional protective buffer;
- a target loan to deposit ratio of 122.5% by 2013 through a combination of run-off and disposal of non-core assets;
- AIB will have to raise total equity capital of € 13.3 billion (€10.5 billion plus €2.8 billion capital buffer) of which €1.4 billion may be in the form of contingent capital.

Following on this report, the Minister for Finance announced on 31 March 2011 a restructuring of the Irish banking system. This restructuring revolves around two pillar banks, with AIB and EBS merging in the coming months (subject to State aid and regulatory approvals) to form one of these pillar banks. The non-core division of the combined entity will be required to deleverage assets to achieve the target loan to deposit ratio.

The Government has signalled its support for the recapitalisation of the Irish banks, which in total amounts to €24 billion, to ensure that the Irish banking system is returned to health. It has also signalled that it will seek direct contributions to solving the capital issues of the banking system by requiring further significant contributions from other sources, including from subordinated debt holders, by the sale of assets to generate capital and where possible, by seeking private sector investors. In its announcement, the Government reconfirmed that all deposits remain fully guaranteed by the State under the deposit guarantee scheme and the ELG scheme.

Share capital injection
In February 2011, €340m of share capital was injected into AIB Mortgage Bank by its parent, Allied Irish Banks, p.l.c. in order to maintain the regulatory and solvency limits during 2011.

37. Approval of financial statements

The financial statements were approved by the Directors on 26 April 2011.