



QIB (UK) plc

Annual Report

For the year ended 31 December 2012

Registered number 4656003

THURSDAY



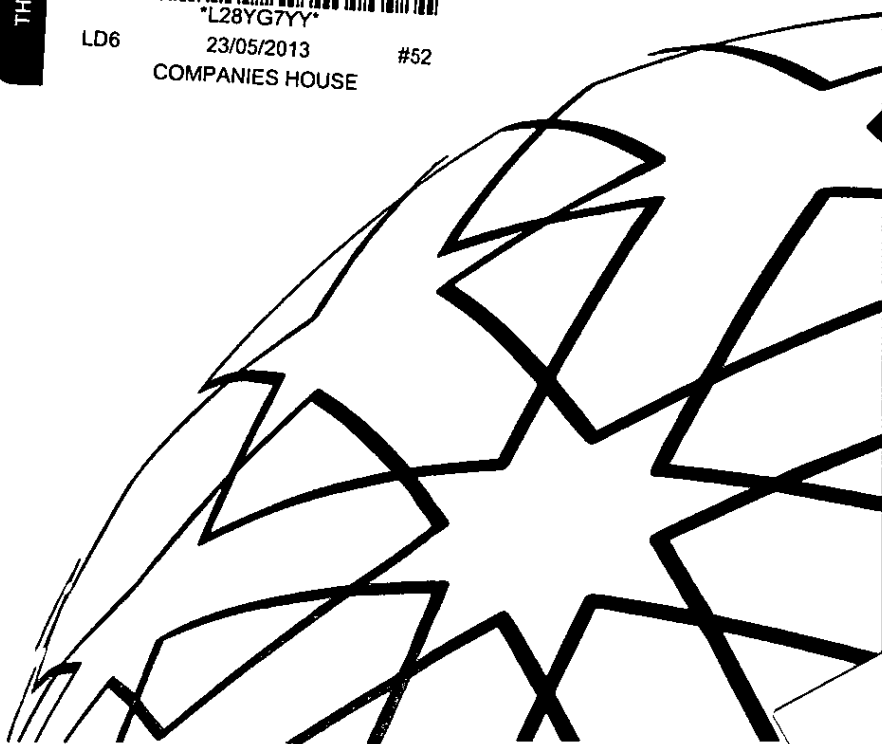
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## Directors' Report

The Directors present their report and the audited financial statements for the year ended 31 December 2012

### Principal activities

QIB (UK) plc (the 'Company' or the 'Bank'), was incorporated with the intention of developing and offering Shari'a compliant financial products and solutions in the UK and Europe and to attract investment into these markets from the Gulf and Middle East. The Company received authorisation from the Financial Services Authority (FSA) on 29 January 2008 after which date it commenced operations as a Shari'a compliant investment bank in line with the objectives stated above.

### Financial results

The financial statements for the year ended 31 December 2012 are shown on pages 11 to 50. The loss for the year is £3,438,945 (2011 profit of £91,338).

### Business review

2012 represented a key year in the Bank's development. It was the fifth year of operations since the Bank's authorisation and this was reflected in solid underlying income growth across the majority of the Bank's core business lines, as product offerings in a number of areas reached initial maturity.

Operating income for the Bank increased by 9.2% in 2012 to £8,001,119 (2011 £7,326,977). Expenses of £6,931,606 were lower than the prior year comparable total of £6,949,433, resulting in a profit before impairment-related costs of £1,069,513 (2011 £377,544).

However, the Bank's result for the year was significantly impacted by specific impairment provisions and fair value losses relating to impaired assets of £5,179,255 on two corporate financing exposures originated in previous years. This is discussed further in the Corporate Finance section below.

The Bank's main business lines remain as Asset Management, Corporate Finance, Real Estate and Treasury.

#### *Asset Management*

The Asset Management division continued to develop its product offering with the aim of providing a wide range of Shari'a compliant investment solutions to clients including high net worth individuals, sovereign wealth funds and institutional investors.

It was a positive year for the Global Sukuk Plus Fund managed by the Bank. The fund continued to perform well with the annual return of 8.6% in the year exceeding its marketed benchmark. The cumulative return since the fund's inception in March 2009 has been 30.0%. This positive track record has made the fund more attractive to new investors and there has been solid growth in the total fund size, which was £134,974,790 as at 31 December 2012 (2011 £111,903,061).

During 2012, sales effort was focused primarily on the Sukuk fund. Consequently, the other funds managed by the Bank did not experience asset growth but provided positive returns. The Islamic Financial Institution Fund was fully launched during 2011 with the objective of investing in the equity of listed Shari'a compliant financial institutions. As at 31 December 2012, the fund size was £14,401,809 (2011 £17,448,771). This reduction was due to a redemption by a particular client wishing to reallocate funds and actual fund performance was positive. In late 2011, the Bank had also launched the Qatar Opportunities Fund. This fund will invest in equities exposed directly to the period of forecast growth in Qatar. There will be further focus on the growth of these funds in 2013.

Additional structured note products were also launched during the year, offering investors the opportunity to obtain returns linked to the performance of different stock markets over a fixed period, whilst also offering capital protection. Three previous notes offered by the Bank matured in 2012, returning 10.1%, 16.9% and 6.4% over each of their respective two-year note periods.

## Directors' Report (continued)

The future focus for Asset Management is to further grow each of the funds and also to develop a wealth management proposition, offering clients a range of investment solutions

### *Corporate Finance*

Activities include the provision of Shari'a compliant financing and advice and arrangement relating to private equity, mergers and acquisitions and business development. The division successfully completed both advisory and financing transactions with a number of counterparties during the year.

However, the business line was impacted significantly by impairment-related losses incurred during the year. The most significant of these was as a result of a UK retail operation that had been financed by the Bank in 2010 entering administration, due to an ongoing trading slowdown in the current economic climate. This resulted in a full impairment of £1,500,000 against equity options in the entities and a full impairment provision against outstanding financing of £3,377,957. Additionally, the provision against an exposure to a Middle Eastern corporate was increased from 80% to 100%, resulting in an additional impairment charge in the year of £301,298.

On the positive side, an equity interest in a company was obtained during the year as payment for business development and advisory services provided to a financial structuring company. This equity interest was independently valued at £2,036,751 as at 31 December 2012. The Bank also holds an equity interest in a technology and media company which has developed multi-media public recycling facilities to be installed in major cities. The company has already secured a contract with the City of London and during the year operations went live. The company is demonstrating good progress in obtaining further contracts in other cities and is now at the stage of positive income generation. The development of the business over the year resulted in an increase in the valuation of the Bank's interest, as independently valued, to £2,017,402 (2011: £1,900,693). The Bank holds a further option over the equity of a pharmaceutical research company, involved in pioneering research and development using emerging technology. This option was independently valued at £188,840 as at 31 December 2012 (2011: £nil).

These equity interests provide potential for further positive revaluation gains over future years, as the underlying companies continue to develop. There is also a potential risk of the value of the companies falling below the amount recognised as at 31 December 2012. The Bank continues to monitor the companies closely to ensure that progress is in line with plans.

The Bank is currently completing a full review of its Corporate Finance business line, to develop the future strategy and determine core activities for the next five years.

### *Real Estate*

The Bank's Real Estate team provides a range of services including specialist property related advice and consultancy, Shari'a compliant financing and asset management of property investments.

Over the last two years, the Bank has taken advantage of favourable Real Estate financing conditions as traditional Real Estate financiers have sought to reduce exposure to the sector. During this period the Bank has built a good quality portfolio of Musharaka and Murabaha financings. Total Real Estate financing as at 31 December 2012 was £34,932,109 (2011: £25,310,328).

During the year, the Bank also secured asset management income by arranging for co-investors to sub-participate in a number of large development and residential investment financing transactions. The Real Estate team also provided consultancy and advisory services relating to the arrangement of Shari'a compliant financing provided by other parties.

The future plans for the Real Estate business line include the launch of Real Estate investment funds.

## Directors' Report (continued)

### *Treasury*

The Treasury division is responsible for managing the Bank's balance sheet in accordance with FSA guidelines and Shari'a principles, as well as maximising profit from trading in various Shari'a compliant investment products. During the year, the positive gains on the investment portfolio maintained by Treasury were £1,472,227 (2011: £730,919), driven by investments in the Sukuk market. It is recognised that the potential for such gains is dictated by market conditions and Treasury is focused on expanding its future income base, by developing a range of Shari'a compliant treasury and currency related products.

### *Looking ahead*

The Board is currently working closely with the Bank's parent company, Qatar Islamic Bank, to finalise a capital increase in the early part of 2013. This increase coincides with a strategic review to set the Bank's direction for the next five years. The strategic review will consider the optimum product offerings in each of the Bank's business lines to build upon the foundations that have been built in the first five years of operation.

A detailed explanation of the Bank's approach to financial and operational risk management is set out in note 28 to the financial statements. As the Bank has developed, the level of key performance indicator ('KPI') review has also increased. In addition to reviewing financial measures such as return on equity, management has implemented more detailed scorecards to monitor operational efficiency to ensure that operations continue to be enhanced for efficiency and scalability. The KPIs monitored also focus on risk measures to ensure that there is equal focus on effective risk management and the effectiveness of the internal control environment.

### **Proposed dividend**

The Directors do not propose the payment of a dividend (2011: £nil).

### **Directors**

The Directors who held office during the year were as follows:

Sheikh Jassim Bin Hamad J. J. Al Thani (Chairman)  
Professor Abdul Latif Al Meer<sup>1 2</sup>  
Mr Roderick Chamberlain<sup>2</sup>  
Mr Michael Clark<sup>3</sup>  
Mr Salah Jaidah<sup>1</sup>  
Mr Azhar Khan<sup>3</sup>  
Mr David Sambar<sup>1</sup>

- <sup>1</sup> Denotes member of the Remuneration Committee
- <sup>2</sup> Denotes member of the Audit and Risk Committee
- <sup>3</sup> Denotes member of the Executive Committee

Subsequent to the reporting date, the following changes occurred:

Sheikh Jassim Bin Hamad J. J. Al Thani	Resigned on 15 January 2013
Professor Abdul Latif Al Meer	Resigned on 15 January 2013
Mr Salah Jaidah	Resigned on 15 January 2013
Mr David Sambar	Resigned on 15 January 2013
Mr Ahmad Meshari (Chairman)	Appointed on 15 January 2013
Mr Giles Cunningham	Appointed on 15 January 2013
Mr Bert de Ruiter	Appointed on 15 January 2013
Mr David Thomas	Appointed on 15 January 2013

## Directors' Report (continued)

### Shari'a Supervisory Committee members

As a Shari'a compliant bank, the Company's governance structure includes a Shari'a Supervisory Committee (SSC) which is responsible for overseeing that all products and activities of the Bank are Shari'a compliant. The SSC has no Executive responsibilities. The SSC members throughout the year were as follows:

Sheikh Walid Ben Hadi (Chairman)  
Sheikh Nizam Mohammed Yacoubi  
Professor Abdul Sattar Abou Ghodda

The annual report of the SSC is shown on page 8.

### Creditor payment policy

The Company's policy is to agree terms and payment conditions before business is transacted and to pay creditors in line with those terms. As a Shari'a compliant bank, the Company is not permitted to pay any interest charges and therefore all invoices are paid in line with agreed terms to ensure that late payment charges are not incurred.

### Political and charitable contributions

The Company made no political contributions (2011: £nil) or charitable donations (2011: £nil) during the year.

### Going concern

The Directors have reviewed the current and potential future business activities and financial position of the Company, including an assessment of capital and liquidity requirements for the foreseeable future. Qatar Islamic Bank, the Company's parent, has confirmed its ongoing financial support to the Company whenever needed. Based on this review, the Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future and therefore the financial statements have been prepared on a going concern basis.

### Disclosure of information to auditors

The Directors who held office at the date of approval of this Directors' Report confirm that, as far as each of them is aware, there is no relevant audit information of which the Company's auditors are unaware, and each Director has taken all the steps that he ought to have taken as a Director to make himself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

By order of the Board



Azhar Khan  
Company Secretary  
15 January 2013

4<sup>th</sup> Floor  
Berkeley Square House  
Berkeley Square  
London  
W1J 6BX

## Statement of Directors' Responsibilities

The Directors are responsible for preparing the Directors' Report and the financial statements in accordance with applicable law and regulations

Company law requires the Directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union (EU) and applicable law.

Under company law the Directors must not approve the financial statements unless they are satisfied that they present fairly the financial position and performance of the Company for that period.

In preparing these financial statements, the Directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgements and accounting estimates that are reasonable and prudent,
- state whether they have been prepared in accordance with IFRSs as adopted by the EU, subject to any material departures disclosed and explained in the financial statements, and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors confirm that they have complied with the above requirements in preparing the financial statements.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that its financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking steps to prevent and detect fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

## Shari'a Supervisory Committee Report

In the name of Allah, the Most Gracious, the Most Merciful

To the shareholders of QIB (UK) plc (the 'Company')

For the year ended 31 December 2012

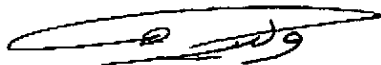
In compliance with the Terms of Reference of the Company's Shari'a Supervisory Committee, we submit the following report

We have reviewed the accounts relating to the transactions entered into by the Company during the year ended 31 December 2012

Based on our review, and representations received from the Company's management, all transactions during the period were on the basis of agreements approved by us

Therefore, in our opinion the transactions entered into by the Company during the year ended 31 December 2012 are in compliance with the Islamic Shari'a rules and principles and fulfil the specific directives, rulings and guidelines issued by us

We beg Allah the Almighty to grant us all success



**Sheikh Walid Ben Hadi**  
Chairman of the Shari'a Supervisory Committee  
15 January 2013



## **Independent Auditors' Report to the Members of QIB (UK) plc**

We have audited the financial statements of QIB (UK) plc (the 'Company') for the year ended 31 December 2012 which comprise the Statement of Comprehensive Income, the Balance Sheet, the Statement of Changes in Equity, the Statement of Cash Flows and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

### **Respective responsibilities of directors and auditors**

As explained more fully in the Directors' Responsibilities Statement set out on page 7, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

### **Scope of the audit of the financial statements**

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the Company's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors, and the overall presentation of the financial statements.

### **Opinion on financial statements**

In our opinion the financial statements

- give a true and fair view of the state of the Company's affairs as at 31 December 2012 and of its loss and cash flows for the year then ended,
- have been properly prepared in accordance with IFRSs as adopted by the European Union, and
- have been prepared in accordance with the requirements of the Companies Act 2006

**Opinion on other matter prescribed by the Companies Act 2006**

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements

**Matters on which we are required to report by exception**

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us, or
- the financial statements are not in agreement with the accounting records and returns, or
- certain disclosures of directors' remuneration specified by law are not made, or
- we have not received all the information and explanations we require for our audit



Darren Meek (Senior Statutory Auditor)  
For and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
7 More London Riverside  
London SE1 2RT  
Date 17 January 2013

## Statement of Comprehensive Income

For the year ended 31 December 2012

	Note	2012 £	2011 £
<b>Income</b>			
Income from financing and investing activities	4	5,540,799	2,644,263
Returns to banks and customers	5	<u>(3,299,437)</u>	<u>(1,187,821)</u>
<b>Net income from financing and investing activities</b>		<u>2,241,362</u>	<u>1,456,442</u>
 Fees and commissions income	6	4,420,906	5,797,976
Fees and commissions expense		<u>(316,825)</u>	<u>(538,322)</u>
<b>Net fees and commissions income</b>		<u>4,104,081</u>	<u>5,259,654</u>
 Net gains on financial assets classified as held for trading		1,472,227	730,919
Gain / (loss) on foreign exchange		1,008,126	(944,406)
Fair value gain / (loss) on forward foreign exchange	16	<u>(824,677)</u>	<u>824,368</u>
 <b>Total operating income</b>		<u>8,001,119</u>	<u>7,326,977</u>
 <b>Expenses</b>			
Personnel expenses	7	(3,990,183)	(3,936,964)
Depreciation and amortisation	18, 19	(199,111)	(286,996)
Other expenses		<u>(2,742,312)</u>	<u>(2,725,473)</u>
<b>Total operating expenses before impairment and related fair value loss</b>		<u>(6,931,606)</u>	<u>(6,949,433)</u>
 <b>Profit before impairment and related fair value loss</b>		1,069,513	377,544
Provisions for impairment	28	(3,679,255)	(113,605)
Fair value loss related to impaired assets	16	<u>(1,500,000)</u>	<u>-</u>
 <b>Profit / (loss) before taxation</b>		<u>(4,109,742)</u>	<u>263,939</u>
 Taxation	9	670,797	(172,601)
 <b>Profit / (loss) for the year</b>		<u>(3,438,945)</u>	<u>91,338</u>
 <b>Other comprehensive income</b>			
Net change in fair value of AFS financial assets	17	305,549	-
 <b>Total comprehensive profit / (loss) for the year</b>		<u>(3,133,396)</u>	<u>91,338</u>

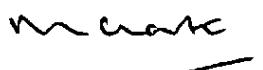
All activities are derived from continuing operations. The notes on pages 15 to 50 are an integral part of these financial statements.

**Balance Sheet**  
**As at 31 December 2012**

	Note	2012 £	2011 £
<b>Assets</b>			
Cash and balances with banks	10	4,626,245	1,455,093
Due from banks	11	71,412,705	52,361,914
Financing arrangements	12	52,464,110	36,735,640
Less impairment on financing arrangements	28	(5,279,916)	(1,600,661)
Financial assets held for trading	14	25,827,202	27,006,222
Financial assets held to maturity	15	7,446,552	4,210,887
Financial assets available for sale	17	4,242,993	1,900,693
Derivative financial instruments	16	(309)	2,324,368
Property and equipment	18	467,184	600,158
Intangible assets	19	63,651	49,195
Other assets	20	4,279,507	3,638,142
Deferred tax asset	9	3,037,095	2,366,298
<b>Total assets</b>		<b>168,587,019</b>	<b>131,047,949</b>
<b>Liabilities</b>			
Due to banks	21	43,528,523	25,901,549
Due to customers	22	102,819,363	81,119,886
Loan from related party	27	-	4,757,834
Other liabilities	23	3,540,475	2,194,460
Subordinated loan	27	4,757,834	-
<b>Total liabilities</b>		<b>154,646,195</b>	<b>113,973,729</b>
<b>Equity</b>			
Share capital	26	25,000,001	25,000,001
Fair value reserve on AFS financial assets	17	305,549	-
Retained deficit		(11,364,726)	(7,925,781)
<b>Total equity</b>		<b>13,940,824</b>	<b>17,074,220</b>
<b>Total liabilities and equity</b>		<b>168,587,019</b>	<b>131,047,949</b>

The notes on pages 15 to 50 are an integral part of these financial statements

These financial statements were approved by the Board of Directors and were signed on its behalf by

  
**Michael Clark**  
Chief Executive Officer

  
**Azhar Khan**  
Chief Financial Officer

QIB (UK) plc  
Registered number 4656003

**Statement of Changes in Equity**  
For the year ended 31 December 2012

	Share Capital	Fair Value Reserve on AFS Financial Assets	Retained Earnings	Total
	£	£	£	£
Balance at 1 January 2011	25,000,001	-	(8,017,119)	16,982,882
Net Change in fair value of AFS financial assets	-	-	-	-
Profit for the year after tax	-	-	91,338	91,338
Balance at 31 December 2011	<u>25,000,001</u>	<u>-</u>	<u>(7,925,781)</u>	<u>17,074,220</u>
Balance at 1 January 2012	25,000,001	-	(7,925,781)	17,074,220
Net Change in fair value of AFS financial assets	-	305,549	-	305,549
Loss for the year after tax	-	-	(3,438,945)	(3,438,945)
Balance at 31 December 2012	<u>25,000,001</u>	<u>305,549</u>	<u>(11,364,726)</u>	<u>13,940,824</u>

The notes on pages 15 to 50 are an integral part of these financial statements

## Statement of Cash Flows

For the year ended 31 December 2012

	<i>Note</i>	2012 £	2011 £
<b>Cash flows from operating activities</b>			
(Loss) / profit for the year		(3,438,945)	91,338
Adjustments for			
Depreciation	18	164,489	183,157
Amortisation	19	34,622	103,839
Taxation	9	(670,797)	172,601
Impairment provision	28	3,679,255	113,605
Increase in amounts due from banks		(19,050,791)	(37,056,370)
Increase in financing arrangements		(15,728,470)	(12,124,564)
(Increase) / decrease in other assets		(641,365)	1,423,639
Increase in amounts due to banks		17,626,974	25,996
Increase in amounts due to customers		21,699,477	69,686,573
Increase in other liabilities		1,346,015	1,100,086
Decrease / (increase) in financial assets held for trading		1,179,020	(15,799,667)
Increase in financial assets held to maturity		(3,235,665)	(4,210,887)
Increase in financial assets available for sale		(2,036,751)	(1,900,693)
Decrease / (increase) in derivative financial instruments		2,324,677	(2,324,368)
<b>Net cash inflow / (outflow) from operating activities</b>		<b>3,251,745</b>	<b>(515,715)</b>
<b>Cash flows from investing activities</b>			
Purchase of property and equipment	18	(31,515)	(39,114)
Purchase of intangible assets	19	(49,078)	(22,674)
<b>Net cash outflow from investing activities</b>		<b>(80,593)</b>	<b>(61,788)</b>
<b>Net increase / (decrease) in cash and cash equivalents</b>		<b>3,171,152</b>	<b>(577,503)</b>
Cash and cash equivalents at start of year		1,455,093	2,032,596
<b>Cash and cash equivalents at end of year</b>	10	<b>4,626,245</b>	<b>1,455,093</b>

The notes on pages 15 to 50 are an integral part of these financial statements

## Notes to the Financial Statements

### 1. Reporting entity

QIB (UK) plc (the 'Company' or the 'Bank') is incorporated and domiciled in the UK. The address of the Company's registered office is 4<sup>th</sup> Floor, Berkeley Square House, Berkeley Square, London W1J 6BX. The Company operates as a Shari'a compliant investment bank.

### 2. Basis of preparation

#### a. Statement of compliance

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU, IFRIC Interpretations and the Companies Act 2006 applicable to companies reporting under IFRS.

The financial statements were approved by the Board of Directors on 15 January 2013.

The accounting policies set out below have, unless otherwise stated, been applied consistently to all the years presented in these financial statements.

#### b. Basis of measurement

The financial statements have been prepared under the historical cost convention, except financial assets held at fair value through profit or loss and available for sale financial assets which have been measured at fair value.

#### c. Functional and presentation currency

The financial statements are presented in Sterling, which is the Company's functional currency.

#### d. Use of estimates and judgements

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

The key sources of estimation uncertainty are:

##### (i) Provisions for impairment of financial assets

A financial asset is considered to be impaired if there is objective evidence of events since initial recognition of the asset that will adversely affect the amount or timing of future cash flows from the asset. The amount of the impairment loss will be the difference between the carrying value of the financial asset and the present value of the estimated future cash flow. In estimating these cash flows, management makes judgements about each counterparty's financial situation and the realisable value of any underlying collateral or any other means of repayment.

##### (ii) Impairment of non-financial assets

At each reporting date the Company reviews the carrying value of its non-financial assets, specifically property and equipment and intangible assets, to determine whether there is any indication that these assets have suffered an impairment loss. If any such indication exists the recoverable amount of the asset is estimated in order to determine the extent of any impairment loss. The recoverable amount for property and equipment and intangible assets is based on an estimation of the continuing use of the assets in the business.

## Notes to the Financial Statements

### (iii) Determining fair values

The determination of fair value for financial assets and liabilities for which there is no observable market price may require the use of valuation techniques, based on variables that may include data not directly from observable markets. For financial instruments that trade infrequently and have little price transparency, fair value is less objective and requires varying degrees of judgement depending on liquidity, concentration, uncertainty of market focus, pricing assumptions and other risks affecting the specific instrument.

### (iv) Recognition of deferred tax asset

Deferred income tax assets are recognised for tax loss carry-forwards to the extent that the realisation of the related tax benefit against future taxable profits is probable. In making this decision, business projections are reviewed in detail and stress-tested to assess the probable likelihood of such recovery.

### (v) Recoverability of VAT

HMRC has agreed the partial exemption special method for VAT recoverability with HMRC. This follows detailed discussions with HMRC relating to the VAT treatment of specific Islamic products. The amount of recoverable VAT recognised represents the expected amount recoverable based on the method agreed by HMRC.

## e Going concern

The Directors have reviewed the current and potential future business activities and financial position of the Company, including an assessment of capital and liquidity requirements for the foreseeable future. Qatar Islamic Bank, the Company's parent, has confirmed its ongoing financial support to the Company whenever needed. Based on this review, the Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future and therefore the financial statements have been prepared on a going concern basis.

## 3 Significant accounting policies

### a Financial instruments

(i) Murabaha is a contract for the sale of goods at cost plus an agreed profit mark-up. The delivery of the goods from the seller to the purchaser is immediate but payment may be deferred. Such contracts may be used to provide financing. Commodity Murabaha is a specific example of such a contract where the item being sold is a metal commodity. Commodity Murabaha contracts are commonly used within the Islamic inter-bank short-term liquidity market.

(ii) Wakala is a transaction, which represents an agreement whereby a party provides a certain sum of money to an agent, who invests it according to specific conditions in order to achieve a certain specified return. The agent is obliged to return the invested amount in case of default, negligence or violation of any of the terms and conditions of the Wakala.

(iii) Istisna is a contract for the acquisition of a product or property which is not in existence at the start of the contract and is built or manufactured according to detailed specifications defined by the client and delivered at the agreed date and price. Istisna contracts are used within financing activities.

(iv) Ijara is a contract granting the right to use an asset by one party to another which equates to the leasing of the asset in return for rental payments, and which may include a transfer of ownership title at the end of the rental period. Ijara contracts are typically used for medium to long term financing of equipment, plant and machinery and vessels or aircraft.

(v) Mudaraba is a partnership contract in which a provider of capital enters into an agreement with a partner to undertake a specific business or project. Profits are shared on a pre-agreed basis but losses are borne by the provider of capital unless negligence of the partner, who typically provides the labour or expertise, is demonstrated.



## Notes to the Financial Statements

(vi) Wa'ad is a purchase undertaking by one party to the other in a transaction effectively resulting in either a right to acquire or sell for one of the parties, structured with Shari'a compliant conditions. A Wa'ad could be an available for sale asset where it does not meet the definition of a derivative or could be a derivative recognised at fair value.

The above contracts form the basis of financial instruments shown within due from banks, financing arrangements, and due to banks and customers.

These financial instruments are recognised on the trade date, that is, the date on which there is a commitment to buy or sell the financial instrument. The resulting assets and liabilities are initially recorded at fair value and are subsequently measured at amortised cost.

Income and costs on the above financial instruments are recognised on an effective yield basis. The effective yield rate is the rate that exactly discounts the estimated future cash payments and receipts through the agreed payment term of the contract to the carrying amount of the receivable or payable. The effective yield is established on initial recognition of the asset or liability and is not revised subsequently. Accrued income receivable and returns payable are included within other assets and other liabilities.

The calculation of the effective yield rate includes all fees paid or received, transaction costs, and discounts or premiums that are an integral part of the effective yield rate. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or liability.

Financial assets and liabilities are offset and the net amount is reported in the Balance Sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

### **b Financial assets at fair value through profit and loss**

Financial assets at fair value through profit or loss comprises two sub-categories: financial assets classified as held for trading, and financial assets designated by the Company as at fair value through profit or loss upon initial recognition.

A financial asset is classified as held for trading if it is acquired or incurred principally for the purpose of selling or repurchasing it in the near term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. Financial assets held for trading consist of investments in quoted Sukuk, managed funds and structured notes and are recognised in the Balance Sheet as 'Financial assets held for trading'.

Financial instruments included in this category are recognised initially at fair value, transaction costs are taken directly to the Statement of Comprehensive Income. Gains and losses arising from changes in fair value are included directly in the Statement of Comprehensive Income and are reported as 'Net gains / (losses) on financial assets classified as held for trading'. The investments are derecognised when the rights to receive cash flows have expired or the Company has transferred substantially all the risks and rewards of ownership and the transfer qualifies for derecognition.

### **c Held to maturity financial investments**

Held to maturity investments are measured at amortised cost using the effective yield basis. The Bank assesses all held to maturity investments for impairment on each reporting date. If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying value and present value of future cash flows discounted using the original effective yield rate. The carrying amount of the asset is reduced and the loss is recognised in the Statement of Comprehensive Income. If the impairment loss decreases (or there is objective evidence that the loss has decreased) after the impairment was recognised, then the corresponding impairment is reversed through the Statement of Comprehensive Income.

## Notes to the Financial Statements

### **d Financial assets available for sale**

Financial assets available for sale are initially recognised at fair value. Subsequent to initial measurement, the fair value gain or loss on these assets is reported into the Statement of Changes in Equity. On sale or impairment of the asset, the cumulative gain or loss previously recognised in the Statement of Changes in Equity is reclassified into the Statement of Comprehensive Income.

### **e Derivative financial instruments**

Derivative financial instruments include Islamic contracts based on the Wa'ad principle of Islamic financing and forward foreign exchange contracts. Derivative financial instruments are initially recognised at fair value. Subsequently, these instruments are measured at fair value with changes in fair value recognised in the Statement of Comprehensive Income.

### **f Property financing**

Property finance is provided using the Musharaka (partnership) principle of Islamic financing. The Company will enter into an agreement to jointly purchase a property with another party and rental income will be received relating to that proportion of the property owned by the Company at any point in time. The other party to the agreement may make separate payments to purchase additional proportions of the property from the Company, thereby reducing the Company's effective share.

The transaction is recognised as a financial asset upon legal completion of the property purchase and the amount receivable is recognised at an amount equal to the net investment in the transaction. Where initial direct costs are incurred by the Company such as commissions and legal fees that are incremental and directly attributable to negotiating and arranging the transaction, these costs are included in the initial measurement of the receivable and the amount of income over the term will be reduced. Rental income is recognised at a constant periodic rate of return on the Company's net investment.

### **g Derecognition of financial assets and liabilities**

Financial assets are derecognised when the contractual rights to the cash flows from the asset expire, or the Company transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any remaining interest in transferred financial assets that is created or retained by the Company is recognised as a separate asset or liability.

The Company derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

### **h Impairment of financial assets**

At each reporting date it is assessed whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash flows from the asset that can be estimated reliably.

All individually significant financial assets are assessed for specific impairment. Objective evidence that financial assets are impaired include default or delinquency by the counterparty, extending or changing repayment terms, indications that a counterparty may go into bankruptcy, or other observable data relating to a group of assets such as adverse changes in the payments status of counterparties, or economic conditions that correlate with defaults in the Company.

Impairment losses on assets carried at amortised cost are measured as the difference between the carrying amount of the financial asset and the present value of the estimated cash flows discounted at the assets' original

## Notes to the Financial Statements

effective yield rate. Losses are recognised in the Statement of Comprehensive Income and reflected against the asset carrying value. When a subsequent event causes the amount of impairment losses to decrease, the impairment loss is reversed through the Statement of Comprehensive Income.

In the case of equity interests and investments classified as available for sale, a significant or prolonged decline in the fair value of the security below its cost is also evidence that the assets are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in profit or loss. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement.

### **i Impairment of non-financial assets**

The carrying amounts of non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated. An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets and groups. Impairment losses are recognised in the Statement of Comprehensive Income.

The recoverable amount of an asset is the greater of its value in use and its fair value less costs to resell. In assessing value in use, the estimated future cash flows are discounted to their present value. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

### **j Provisions**

A provision is recognised if, as a result of a past event, the Company has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of cost of funds and, where appropriate, the risks specific to the liability.

### **k Fees and commissions**

Fees and commissions which are not recognised on an effective yield basis over the life of the financial instrument to which they relate are recognised at the point when any specific actions or events relating to the payment of the fees or commissions have been completed and the fees and commissions are earned.

### **l Property and equipment**

Items of property and equipment are measured at cost less accumulated depreciation and impairment losses. Cost includes expenditure that is directly attributable to the acquisition of the asset.

The cost of replacing part of an item of property or equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Company and its cost can be measured reliably. The costs of the day-to-day servicing of property and equipment are recognised in the Statement of Comprehensive Income as incurred.

Depreciation is recognised in the Statement of Comprehensive Income on a straight line basis over the estimated useful life of each part of an item of property and equipment. Depreciation methods, useful lives and residual values are reassessed at the reporting date.

## Notes to the Financial Statements

The current estimated useful lives are as follows

Computer equipment	3 Years
Office equipment	5 Years
Fixtures and fittings	5 Years
Leasehold improvements	10 Years

### m Intangible assets

Acquired software and computer licenses are stated at cost less accumulated amortisation and accumulated impairment losses. Expenditure on internally developed software is recognised as an asset when the Company is able to use the software in a manner that will generate future economic benefits, and can reliably measure the costs to complete the development.

Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure, including expenditure on internally generated goodwill and brands, is recognised in the Statement of Comprehensive Income as incurred.

Amortisation is recognised in the Statement of Comprehensive Income on a straight line basis over the estimated useful lives of intangible assets, other than goodwill, from the date that they are available for use. The current estimated useful lives are as follows:

Software	3 Years
Computer licenses	3 Years

### n Taxation

Income tax payable or receivable is calculated on the basis of the applicable tax law and is recognised as an expense or income for the period, except to the extent that current tax is related to items that are charged or credited directly to equity.

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

Deferred tax is provided in full using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

### o Employee benefits

Obligations for contributions to defined contribution pension plans are recognised as an expense in the Statement of Comprehensive Income when they are due. Short-term employee benefits, such as salaries, paid absences, and other benefits, are accounted for on an accruals basis over the period for which employees have provided services. Bonuses are recognised to the extent that there is a present obligation to employees that can be measured reliably.

## Notes to the Financial Statements

### **p Cash and cash equivalents**

Cash and cash equivalents comprise cash and demand bank deposit accounts and are stated at amortised cost

### **q Other receivables**

Trade and other receivables are stated at their nominal amount less impairment losses

### **r Lease payments made**

Payments made under operating leases are recognised in the Statement of Comprehensive Income on a straight line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

### **s Foreign currency transactions**

Transactions in foreign currencies are translated to the functional currency at exchange rates as at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rate as at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period and the amortised cost in foreign currency translated at the exchange rate at the end of the period. Foreign currency differences arising on translation are recognised in the Statement of Comprehensive Income.

### **t New and amended standards adopted**

There are no IFRSs or IFRIC interpretations that are effective for the first time for the financial year beginning on or after 1 January 2012 that have had a material impact on the Company.

### **u New standards and interpretations not yet adopted**

A number of new standards and amendments to standards and interpretations are effective for annual periods beginning after 1 January 2012, and have not been applied in preparing these financial statements. None of these are expected to have a significant effect on the financial statements of the Company, except the following set out below.

Amendment to IAS 1, 'Financial statement presentation' regarding other comprehensive income. The main change resulting from these amendments is a requirement for entities to group items presented in 'other comprehensive income' (OCI) on the basis of whether they are potentially reclassifiable to profit or loss subsequently (reclassification adjustments). The amendments do not address which items are presented in OCI.

IFRS 13, 'Fair value measurement', aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across IFRSs. The requirements, which are largely aligned between IFRSs and US GAAP, do not extend the use of fair value accounting but provide guidance on how it should be applied where its use is already required or permitted by other standards within IFRSs or US GAAP.

IAS 19, 'Employee benefits', was amended in June 2011. There is no expected impact on the Company.

IFRS 9, 'Financial instruments', addresses the classification, measurement and recognition of financial assets and financial liabilities. IFRS 9 was issued in November 2009 and October 2010. It replaces the parts of IAS 39 that relate to the classification and measurement of financial instruments. IFRS 9 requires financial assets to be classified into two measurement categories: those measured as at fair value and those measured at amortised cost. The determination is made at initial recognition. The classification depends on the entity's

## Notes to the Financial Statements

business model for managing its financial instruments and the contractual cash flow characteristics of the instrument. For financial liabilities, the standard retains most of the IAS 39 requirements. The main change is that, in cases where the fair value option is taken for financial liabilities, the part of a fair value change due to an entity's own credit risk is recorded in other comprehensive income rather than the income statement, unless this creates an accounting mismatch. The Company is yet to assess IFRS 9's full impact and intends to adopt IFRS 9 no later than the accounting period beginning on or after 1 January 2015, subject to endorsement by the EU. The Company will also consider the impact of the remaining phases of IFRS 9 when completed by the Board.

IFRS 10, 'Consolidated financial statements', builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. The standard provides additional guidance to assist in the determination of control where this is difficult to assess. The Company is yet to assess IFRS 10's full impact though intends to adopt IFRS 10 no later than the accounting period beginning on or after 1 January 2013, subject to endorsement by the EU.

IFRS 12, 'Disclosures of interests in other entities', includes the disclosure requirements for all forms of interests in other entities, including joint arrangements, associates, special purpose vehicles and other off balance sheet vehicles. The Company is yet to assess IFRS 12's full impact though intends to adopt IFRS 12 no later than the accounting period beginning on or after 1 January 2013, subject to endorsement by the EU.

There are no other IFRSs or IFRIC interpretations that are not yet effective that would be expected to have a material impact on the Company.

### 4 Income from financing and investing activities

Income from	2012 £	2011 £
<b>Banks</b>		
Murabaha placements	816,201	105,940
Wakala placements	85,673	9,649
<b>Financing arrangements</b>		
Murabaha financing	3,270,349	1,393,875
Wakala financing	87	27,893
Musharaka financing	412,397	314,286
Mudaraba financing	100,193	35,739
Ijara financing	68,988	92,935
<b>Other</b>		
Foreign exchange spot transactions	(68,855)	(7,449)
Returns on investments	855,766	671,395
<b>Total income from financing and investing activities</b>	<b>5,540,799</b>	<b>2,644,263</b>

## Notes to the Financial Statements

### 5 Returns to banks and customers

	2012 £	2011 £
Murabaha deposits	1,802,023	658,326
Wakala deposits	1,497,414	529,495
Total returns to banks and customers	<u>3,299,437</u>	<u>1,187,821</u>

### 6 Fees and commissions income

	2012 £	2011 £
Advisory and consultancy fees	126,007	2,551,309
Corporate finance fees	1,427,320	403,223
Asset management fees	2,749,462	2,793,487
Other fee income	118,117	49,957
Total fees and commissions income	<u>4,420,906</u>	<u>5,797,976</u>

The Bank acquired a right on a counterparty's shares as compensation for advisory services completed during the year, having obtained a similar right with another counterparty in the prior year. These rights are classified as 'financial assets available for sale' and the initial valuation is recognised within fees and commissions income during the year in which the services for which the right was granted was completed. The initial valuation recognised in the current year is £2,036,751 (2011: £1,900,693).

### 7 Personnel expenses

	2012 £	2011 £
Directors' emoluments and fees	530,000	475,250
Wages and salaries	2,637,607	2,725,371
Social security costs	444,924	363,586
Pension contributions	253,178	235,044
Other staff costs	124,474	137,713
Total personnel expenses	<u>3,990,183</u>	<u>3,936,964</u>

The aggregate of the emoluments in 2012 of the highest paid Director was £235,000 (2011: £202,000) and Company pension contributions of £33,000 (2011: £31,250) were made on his behalf.

The number of employees at the end of the year was 31 (2011: 37) and the average number throughout the year was 33 (2011: 34).

## Notes to the Financial Statements

### 8. Profit / (loss) before taxation

Profit / (loss) before taxation is stated after charging	<b>2012</b>	<b>2011</b>
	<b>£</b>	<b>£</b>
Auditor's remuneration PricewaterhouseCoopers LLP audit services		
Fees payable to Company's auditor for the audit of financial statements	<b>85,875</b>	66,500
Fees payable to Company's auditor for other services		
– other services pursuant to legislation	<b>21,788</b>	30,750
– other services	-	9,000
	<b>107,663</b>	<b>106,250</b>

### 9 Taxation

#### (i) Analysis of total tax expense / (income)

	<b>2012</b>	<b>2011</b>
	<b>£</b>	<b>£</b>
Current tax expense / (income) for current period 24 5% (2011 26 5%)	-	-
Deferred tax expense / (income) relating to		
Origination and reversal of temporary differences	<b>10,243</b>	19,585
Tax losses not utilised / (utilised)	<b>(994,604)</b>	85,115
Effect of tax rate change	<b>244,007</b>	191,279
Prior period adjustment	<b>69,557</b>	(123,378)
Total tax expense / (income)	<b>(670,797)</b>	<b>172,601</b>

#### (ii) Reconciliation of the total tax expense / (income)

The tax income for the year is lower than that resulting from applying the UK standard rate of corporation tax to the profit before tax. The differences are explained as follows:

	<b>2012</b>	<b>2011</b>
	<b>£</b>	<b>£</b>
Profit / (loss) before tax	<b>(4,109,742)</b>	263,939
UK tax at 24 5% (2011 26 5%) thereon	<b>(1,006,887)</b>	69,944
Effects of		
Non-deductible expenses	<b>22,526</b>	34,756
Effect of tax rate change	<b>244,007</b>	191,279
Prior period adjustment	<b>69,557</b>	(123,378)
Total tax expense / (income)	<b>(670,797)</b>	<b>172,601</b>



## Notes to the Financial Statements

### (iii) Deferred tax

Deferred tax is calculated on temporary differences using the tax rate of 23% (2011 25%) The Finance Act 2012 reduced the UK corporation tax rate from 26% to 24% with effect from 1 April 2012, and from 24% to 23% with effect from 1 April 2013 There will be a further 1% reduction in the corporation tax rate to 22% from 1 April 2014 The following are the deferred tax assets recognised by the Company and movements thereon during the current and prior reporting period The Directors are of the opinion, based on forecast trading profits, that it is probable that sufficient future taxable income will be available against which these recognised deferred tax assets can be recovered

	2012 £	2011 £
Deferred tax asset as at 1 January	(2,366,298)	(2,538,899)
Credited to the Statement of Comprehensive Income	(984,361)	104,700
Effect of rate change	244,007	191,279
Prior period adjustment	69,557	(123,378)
Deferred tax asset as at 31 December	<u>(3,037,095)</u>	<u>(2,366,298)</u>

The deferred tax asset can be analysed as follows

Depreciation in excess of capital allowances	(38,408)	(66,967)
Tax losses not utilised	(2,998,687)	(2,295,687)
Unpaid pension costs	-	(3,644)
	<u>(3,037,095)</u>	<u>(2,366,298)</u>

## Notes to the Financial Statements

### 10 Cash and balances with banks

	2012 £	2011 £
Cash	499	817
On demand bank deposits	4,625,746	1,454,276
Total cash and balances with banks	<u>4,626,245</u>	<u>1,455,093</u>

### 11 Due from banks

	2012 £	2011 £
Murabaha placements	56,112,859	32,714,235
Wakala placements	15,299,846	19,647,679
Total due from banks	<u>71,412,705</u>	<u>52,361,914</u>

### 12 Financing arrangements

	2012 £	2011 £
Murabaha financing	34,011,194	23,228,558
Wakala financing	-	195,591
Musharaka financing	14,725,326	8,100,000
Mudaraba financing	3,188,189	3,781,755
Ijara financing	485,187	1,338,648
Other financing	54,214	91,088
Total financing arrangements	<u>52,464,110</u>	<u>36,735,640</u>

## Notes to the Financial Statements

### 13 Finance lease receivables

Assets leased to customers using the Ijara structure, included under financing arrangements, are treated as finance leases. Ijara financing receivables are recognised on the balance sheet and income is recognised over the period of the lease so as to give a constant rate of return on the net cash investment in the Ijara. An Ijara for £326,557 with a UK based corporate due to mature in October 2013, will now terminate earlier as the assets being financed are included within a sale of the company holding the assets to a third party. The following shows the gross investments in Ijara financing receivables

	2012 £	2011 £
Not later than one year	466,270	1,114,696
Later than one year but not later than five years	27,142	329,445
Later than five years	-	-
Gross investment in Ijara financing	<u>493,412</u>	<u>1,444,141</u>
Unearned future rentals	(8,225)	(105,493)
Net investment in Ijara financing	<u>485,187</u>	<u>1,338,648</u>
The net investment in Ijara financing comprises		
Not later than one year	458,252	1,029,809
Later than one year but not later than five years	26,935	308,839
Later than five years	-	-
Total	<u>485,187</u>	<u>1,338,648</u>

### 14 Financial assets held for trading

	2012 £	2011 £
Investment in quoted sukuk	14,088,133	19,370,338
Investment in managed funds	5,355,972	4,374,184
Investment in structured note	6,383,097	3,261,700
Total financial assets held for trading	<u>25,827,202</u>	<u>27,006,222</u>

### 15 Financial assets held to maturity

	2012 £	2011 £
Investment in sukuk	4,485,554	4,210,887
Unquoted fixed-term funds	2,960,998	-
Total financial assets held to maturity	<u>7,446,552</u>	<u>4,210,887</u>

## Notes to the Financial Statements

### 16 Derivative financial instruments

	2012 £	2011 £
Wa'ad	-	1,500,000
Fair value of forward foreign exchange contracts	(309)	824,368
Total derivative financial instruments	<u>(309)</u>	<u>2,324,368</u>

During the prior year, the Bank was granted a Wa'ad (an instrument equivalent to a European call option in economic terms) on 50% of the shares of a UK based corporate, related to the restructuring of financing arrangements. The corporate in whose shares the Wa'ad was issued went into administration during 2012 and the value of the Wa'ad as at 31 December 2012 is £nil (2011 £1,500,000). The Bank entered into forward foreign exchange contracts to manage its foreign currency exposures. The movement in the fair value of forward foreign exchange contracts is included in the Statement of Comprehensive Income and was a loss of £824,677 in the current year (2011 gain of £824,368).

### 17 Financial assets available for sale

	2012 £	2011 £
Value of financial assets available for sale as at 1 January	1,900,693	-
Fair value of Wa'ads upon initial recognition	2,036,751	1,900,693
Increase in fair value after initial recognition	305,549	-
Value of financial assets available for sale	<u>4,242,993</u>	<u>1,900,693</u>

Assets available for sale include rights on a counterparty's shares obtained as compensation for advisory services provided during the year. The fair value of this equity interest as at 31 December 2012, based on an independent valuation which has been completed, was £2,036,751. The Bank was granted two other Wa'ads in the prior year on the shares of two UK based corporates. The fair values of these interests as at 31 December 2012, based on independent valuations of the underlying companies, were £2,017,402 (2011 £1,900,693) and £188,840 (2011 £nil).

## Notes to the Financial Statements

### 18 Property and equipment

	Computer Equipment	Leasehold Improvements	Fixtures & Fittings/Office Equipment	Total
	£	£	£	£
<b>Cost</b>				
Balance at 1 January 2012	334,336	844,618	353,491	1,532,445
Additions	5,625	2,225	23,665	31,515
Balance at 31 December 2012	339,961	846,843	377,156	1,563,960
<b>Depreciation</b>				
Balance at 1 January 2012	(305,023)	(354,387)	(272,877)	(932,287)
Depreciation charge for the year	(20,184)	(84,692)	(59,613)	(164,489)
Balance at 31 December 2012	(325,207)	(439,079)	(332,490)	(1,096,776)
<b>Net book value at 31 December 2012</b>	<b>14,754</b>	<b>407,764</b>	<b>44,666</b>	<b>467,184</b>
<b>Cost</b>				
Balance at 1 January 2011	318,346	839,534	335,451	1,493,331
Additions	15,990	5,084	18,040	39,114
Balance at 31 December 2011	334,336	844,618	353,491	1,532,445
<b>Depreciation</b>				
Balance at 1 January 2011	(275,411)	(270,220)	(203,499)	(749,130)
Depreciation charge for the year	(29,612)	(84,167)	(69,378)	(183,157)
Balance at 31 December 2011	(305,023)	(354,387)	(272,877)	(932,287)
<b>Net book value at 31 December 2011</b>	<b>29,313</b>	<b>490,231</b>	<b>80,614</b>	<b>600,158</b>

## Notes to the Financial Statements

### 19 Intangible assets

	Computer Software £	Computer Licenses £	Total £
Cost			
Balance at 1 January 2012	803,794	394,934	1,198,728
Additions	22,500	26,578	49,078
Balance at 31 December 2012	826,294	421,512	1,247,806
Amortisation			
Balance at 1 January 2012	(755,718)	(393,815)	(1,149,533)
Amortisation charge for the year	(32,918)	(1,704)	(34,622)
Balance at 31 December 2012	(788,636)	(395,519)	(1,184,155)
<b>Net book value at 31 December 2012</b>	<b>37,658</b>	<b>25,993</b>	<b>63,651</b>
Cost			
Balance at 1 January 2011	781,395	394,659	1,176,054
Additions	22,399	275	22,674
Balance at 31 December 2011	803,794	394,934	1,198,728
Amortisation			
Balance at 1 January 2011	(660,807)	(384,887)	(1,045,694)
Amortisation charge for the year	(94,911)	(8,928)	(103,839)
Balance at 31 December 2011	(755,718)	(393,815)	(1,149,533)
<b>Net book value at 31 December 2011</b>	<b>48,076</b>	<b>1,119</b>	<b>49,195</b>

### 20 Other assets

	2012 £	2011 £
Income receivable	2,146,546	929,148
Fees receivable	460,849	984,898
VAT recoverable	882,870	819,250
Prepayments	339,431	285,598
Other receivables	449,811	619,248
<b>Total other assets</b>	<b>4,279,507</b>	<b>3,638,142</b>

HMRC has now agreed the Company's partial exemption special method for VAT recoverability. This follows detailed discussions with HMRC relating to the VAT treatment of specific Islamic products. VAT recoverable in the current year is the expected calculated recovery based on the method agreed with HMRC. In the prior year, the method was yet to be agreed by HMRC and total VAT recoverable was net of a provision of £200,000 to reflect estimated non-recovery of an element of VAT.

## Notes to the Financial Statements

### 21. Due to banks

	2012 £	2011 £
Demand	77,032	56,111
Murabaha deposits	912,681	-
Wakala deposits	42,538,810	25,845,438
Total due to banks	<u>43,528,523</u>	<u>25,901,549</u>

### 22 Due to customers

	2012 £	2011 £
Demand	4,096,485	1,328,754
Murabaha deposits	77,218,468	46,790,046
Wakala deposits	21,504,410	33,001,086
Total due to customers	<u>102,819,363</u>	<u>81,119,886</u>

### 23 Other liabilities

	2012 £	2011 £
Returns payable	2,615,130	958,782
Accruals	243,561	527,600
Trade payables	134,279	46,911
Social security and income tax	140,663	116,374
Other payables	406,842	544,793
Total other liabilities	<u>3,540,475</u>	<u>2,194,460</u>

### 24 Commitments under operating lease

There is a commitment at the year-end under a non-cancellable lease for the Company's main premises at 4<sup>th</sup> Floor, Berkeley Square House, Berkeley Square, London W1J 6BX for a 15 year period from 5 April 2007, at an annual rental of £427,840. There is also one lease of duration 10 years 5 months for a car parking space, at an annual rental of £6,500 from 1 November 2011 and two IT rental leases for three years, one for £20,000 per annum from 27 May 2011 and the other for £16,896 per annum from 6 September 2011. The following shows the future minimum lease payments under non-cancellable operating leases

	2012 £	2011 £
Within one year	471,236	470,736
One to five years	1,756,840	1,773,226
More than five years	1,849,891	2,251,728
	<u>4,077,967</u>	<u>4,495,690</u>

During the year £471,812 (2011 £460,477) was recognised as an expense in the Statement of Comprehensive Income in respect of operating leases

## Notes to the Financial Statements

### 25 Contingent liabilities and commitments

	2012 £	2011 £
Letters of credit	-	316,273
Total	<u>-</u>	<u>316,273</u>

Commitments and contingent liabilities stated above do not necessarily represent expected future cash flows as these contracts may expire before actually being drawn

### 26 Share capital

	2012 £	2011 £
<b>Authorised</b>		
50,000,000 Ordinary shares of £1 00 each	<u>50,000,000</u>	<u>50,000,00</u>
<b>Allotted, called up and fully paid</b>		
25,000,001 Ordinary shares of £1 00 each	<u>25,000,001</u>	<u>25,000,001</u>

The details of the shareholders as at 31 December are

	2012	2011
Qatar Islamic Bank	19,000,000	19,000,000
Albidaa LLC	2,500,000	2,500,000
City Capital Limited	2,500,000	2,500,000
Sheikh Jassim Bin Hamad J J Al Thani	250,000	250,000
Mr Salah Jaidah	250,000	250,000
Professor Abdul Latif Al Meer	250,000	250,000
Mr Jean-Marc Riegel	250,000	250,000
Mr Michael Clark	1	1
<b>Total</b>	<u>25,000,001</u>	<u>25,000,001</u>



## Notes to the Financial Statements

### 27 Related party transactions

Qatar Islamic Bank (QIB) is the immediate and ultimate controlling party by virtue of the fact that it holds 76% of the issued share capital and voting rights in the Company. QIB was incorporated on 8 July 1982 as a Qatari shareholding company by the Emiri Decree Number 45 of 1982 to provide banking services, and conduct investment and financing activities in accordance with Islamic Shari'a principles, as determined by its Shari'a Committee and in accordance with the provisions of its Memorandum and Articles of Association.

EFH Funds SCA SICAV SIF ('EFH Funds') is an investment fund vehicle incorporated in Luxembourg as a limited liability partnership. The General Partner of the limited liability partnership is an independent limited company (Sarl) incorporated in Luxembourg. The General Partner acts out of Luxembourg and is responsible for the overall management and governance of the fund. The management board of the Sarl is made up of three managers. The Chief Financial Officer of the Company acts as one of the managers with equal voting rights to each of the other two managers.

There are three active sub-funds that have been launched by EFH Funds, namely, Global Sukuk Plus Fund ('GSPF'), Islamic Financial Institution Fund ('IFI') and Qatar Opportunities Fund ('QOF'). The Bank has been appointed as investment advisor for these funds.

All other related parties are related by virtue of QIB ownership or common Non-Executive Directors, unless otherwise stated below.

#### *Loan from related party*

As at 31 December there was an outstanding loan balance payable to QIB of £4,757,834 (2011 £4,757,834). During the year this loan was converted to tier 2 capital through a subordinated five-year loan structure.

#### *Due to banks*

QIB held demand deposit accounts and entered into Wakala deposit transactions with the Bank on an arm's length basis. As at 31 December, total deposits from QIB were £5,591,119 (2011 £1,990,504). Total returns due to QIB in the year were £68,581 (2011 £206,145) and returns of £14,010 (2011 £890) were payable as at the end of the year. The highest balance of deposits from QIB during the year was £7,475,576 (2011 £19,085,100).

QInvest entered into Wakala deposit transactions with the Bank on an arm's length basis. As at 31 December, total deposits from QInvest were £1,856,091 (2011 £2,394,977). Total returns due to QInvest in the year were £22,431 (2011 £5,347) and returns of £3,243 (2011 £838) were payable as at the end of the year. The highest balance of deposits from QInvest during the year was £6,092,371 (2011 £2,497,191).

#### *Due from banks*

As at 31 December, there were no placements with QIB (2011 £13,883,747). Total returns due in the year from placements with QIB were £48,880 (2011 £6,663) and no returns were receivable as at the end of the year (2011 £1,607). The highest balance of placements with QIB during the year was £3,452,134 (2011 £13,883,747).

#### *Cash and balances with banks*

Demand bank accounts were held with QIB in line with QIB's normal account terms and conditions. As at 31 December, the balance held with QIB was £8,574 (2011 £132).

## Notes to the Financial Statements

### *Due to other institutions*

In the prior year, EFH Funds entered into Wakala deposit transactions with the Bank on an arm's length basis. As at 31 December, no deposits were held from EFH Funds (2011 £5,334,973). Total returns due to EFH Funds in the year were £124,575 (2011 £193,605) and no returns (2011 £97,631) were payable as at the end of the year. The highest balance of deposits from EFH Funds during the year was £5,230,028 (2011 £5,334,973).

### *Financial assets held for trading*

The Bank had the following investments in EFH Funds, shown within assets held for trading, as at 31 December: GSPF £4,855,987 (2011 £3,887,939) and QOF £499,985 (2011 £486,245).

### *Fees and commissions income*

Fund management fees of £1,014,135 (2011 £822,534) were received in relation to GSPF and £102,584 (2011 £259,636) in relation to IFI during the year.

### *Fees receivable*

As at 31 December, fund management fees of £122,829 (2011 £117,760) and £25,197 (2011 £259,636) were receivable from GSPF and IFI respectively relating to the fund management services performed by the Company for the funds during the year.

### *Fees payable*

As at 31 December, amounts of £675 (2011 £665) and £698 (2011 £1,254) were payable to QIB and Arab Finance House ('AFH') respectively, relating to asset management fee rebates. Total rebates due to QIB and AFH in the year were £59,090 (2011 £97,777) and £4,114 (2011 £4,508) respectively.

### *Financing arrangements*

As at 31 December, financing arrangements included a balance of £3,261,699 (2011 £nil) relating to a property Musharaka financing transaction made with Mr Abdullah Al-Eida, a Director of Qatar Islamic Bank, on an arm's length basis. The highest balance during the year for this financing was £3,261,699 (2011 £nil). There was a further Musharaka financing transaction of £3,363,627 (2011 £nil) with Peterson Development Limited, a company related to Mr Al-Eida. The highest balance during the year for this financing was £3,363,627 (2011 £nil). A total of £3,500,000 of these exposures is subject to a sub-participation agreement with an unrelated third party bank.

As at 31 December, financing arrangements included a balance of £21,120 (2011 £25,849) relating to a Murabaha financing transaction made with David Sambar, a Non-Executive Director, on an arm's length basis. The highest balance during the year for this Murabaha financing was £25,849 (2011 £30,259).

### *Bank lines*

As at 31 December the Company had £42,900,452 (2011 £45,000,000) of agreed inter-bank borrowing lines and £24,747,881 (2011 £25,891,643) of agreed lending lines with related parties within the QIB Group. These lines are of varying tenor and duration.

No fees are payable or receivable for these lines and they have been utilised during the year only as described above.

## Notes to the Financial Statements

### *Key management compensation*

Key management of the Company are the Executive Committee. The compensation of key management personnel is as follows:

	2012 £	2011 £
Emoluments including social security costs	528,840	581,000
Company contributions to pension plans	<u>65,250</u>	<u>86,187</u>
	<u>594,090</u>	<u>667,187</u>

As at 31 December, advances totalling £252,722 (2011: £307,955) had been made to key management as part of a staff advance scheme. No returns are payable on these advances and repayment is directly from salary over a maximum period of 5 years or as defined in specific agreements.

## 28 Financial risk management

The Bank monitors and manages exposures to the following risks arising from its use of Islamic financial instruments:

- Capital management
- Credit risk
- Market risk
- Operational risk
- Liquidity risk
- Profit rate risk
- Shari'a compliance risk

This note presents information about the Bank's exposure to each of the above risks and its objectives, policies and processes for identifying, managing and reporting these risks.

### **Risk management framework**

The Board of Directors is ultimately responsible for the management of all risks within the Bank. This includes the establishment and oversight of an overall Risk Management Framework and Corporate Governance Policy which ensure that an appropriate risk management culture is established throughout the Bank.

The Risk Management Framework and Corporate Governance Policy are implemented through the Board's committees, including the Audit and Risk Committee. The day-to-day management of risk is overseen by the Bank's Executive Management Committee ('EXCO') which has established two sub-committees, the Risk Management Committee ('RMC') with responsibility for assessing all credit, market and operational risks, and the Asset and Liability Committee ('ALCO') which is responsible for balance sheet management, and the review and monitoring of profit rate and liquidity risks.

These two sub-committees are responsible for developing suitable policies, approving risks and limits within delegated authorities and regularly reviewing the Bank's exposures to all risk classes. The Bank's Risk Management department ('Risk Management') is responsible for the ongoing operational analysis and review of all the Bank's risks and for providing information to EXCO and the sub-committees. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered.

## Notes to the Financial Statements

### Capital management

The Bank's capital requirements are set and monitored by the FSA. Regulatory capital is analysed in two tiers:

- Tier 1 capital, which includes ordinary share capital and retained earnings
- Tier 2 capital, which includes qualifying subordinated loans

The level of total regulatory capital is monitored against the Individual Capital Guidance. Individual Capital Guidance comprises of Pillar 1 capital using the Standardised Approach and Pillar 2 as required by the FSA. The Bank has complied with all capital requirements throughout the period.

### Credit risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty is not able to repay capital and/or profit, or otherwise meet its contractual obligations under credit facilities or in respect of other agreements.

The Bank has a thorough quantitative and qualitative vetting process in place covering all of its customers and counterparties whereby it assigns an internal risk rating and maximum tenor over and above any external rating. These ratings, which are subject to regular review, control the amount of credit that can be made available to any obligor.

### Management of credit risk

The Bank manages credit risk by monitoring credit exposures, limiting transactions with specific counterparties, countries or sectors and continually assessing the creditworthiness of all counterparties. It also ensures that credit capacities are properly diversified across the Bank's business lines in order to ensure an appropriate allocation of risk capital and to avoid undue concentrations of risk by customer, country, sector or internal ratings.

Risk Management is responsible for the operational management of the Bank's credit risk, including:

- reviewing and approving credit and underwriting proposals, within delegated limits
- reviewing and recommending exceptions to delegated limits, where appropriate
- reviewing, monitoring and actioning, as appropriate, any non-performing credits
- monitoring ongoing adherence to country and counterparty limits

All credit risk exposures are formally approved by the RMC, within delegated limits. Credit risk exposures as at 31 December are shown on the following page.

## Notes to the Financial Statements

	2012 £	2011 £
Balances with banks	4,625,746	1,454,276
Due from banks	71,412,705	52,361,914
Other financing	54,214	91,088
Murabaha financing	34,011,194	23,228,558
Wakala financing	-	195,591
Musharaka financing	14,725,326	8,100,000
Mudaraba financing	3,188,189	3,781,755
Ijara financing	485,187	1,338,648
Financial assets held to maturity	7,446,552	4,210,887
Total	<u>135,949,113</u>	<u>94,762,717</u>
Off-balance sheet		
Letters of credit	-	316,273
Total	<u>-</u>	<u>316,273</u>
Total credit risk	<u>135,949,113</u>	<u>95,078,990</u>

The credit exposures shown above are the maximum credit risk exposures to the Bank without taking account of any collateral held

### *Concentration of risks of financial assets with credit risk exposure*

The following tables provide additional analysis of the credit exposure, showing concentration by geographical location and industry type of counterparties. For geographical sector, allocation of exposures to regions is based on the country of domicile of the counterparty.

## Notes to the Financial Statements

### Geographical sectors

	Europe £	Middle East £	USA £	Other £	Total £
Balances with banks	4,180,980	8,574	436,192	-	4,625,746
Due from banks	35,685,913	17,426,792	14,300,000	4,000,000	71,412,705
Other financing	54,214	-	-	-	54,214
Murabaha financing	32,127,086	1,884,108	-	-	34,011,194
Wakala financing	-	-	-	-	-
Musharaka financing	14,725,326	-	-	-	14,725,326
Mudaraba financing	3,188,189	-	-	-	3,188,189
Ijara financing	485,187	-	-	-	485,187
Financial assets held to maturity	2,960,998	4,485,554	-	-	7,446,552
<b>31 December 2012</b>	<b>93,407,893</b>	<b>23,805,028</b>	<b>14,736,192</b>	<b>4,000,000</b>	<b>135,949,113</b>
Off-balance sheet					
Letters of credit	-	-	-	-	-
<b>31 December 2012</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Total</b>	<b>93,407,893</b>	<b>23,805,028</b>	<b>14,736,192</b>	<b>4,000,000</b>	<b>135,949,113</b>

Balances with banks	1,371,008	8,093	32,975	42,200	1,454,276
Due from banks	25,731,808	26,630,106	-	-	52,361,914
Other financing	91,088	-	-	-	91,088
Murabaha financing	21,257,373	1,971,185	-	-	23,228,558
Wakala financing	195,591	-	-	-	195,591
Musharaka financing	8,100,000	-	-	-	8,100,000
Mudaraba financing	3,781,755	-	-	-	3,781,755
Ijara financing	658,993	679,655	-	-	1,338,648
Financial assets held to maturity	-	-	-	4,210,887	4,210,887
<b>31 December 2011</b>	<b>61,187,616</b>	<b>29,289,039</b>	<b>32,975</b>	<b>4,253,087</b>	<b>94,762,717</b>
Off-balance sheet					
Letters of credit	-	316,273	-	-	316,273
<b>31 December 2011</b>	<b>-</b>	<b>316,273</b>	<b>-</b>	<b>-</b>	<b>316,273</b>
<b>Total</b>	<b>61,187,616</b>	<b>29,605,312</b>	<b>32,975</b>	<b>4,253,087</b>	<b>95,078,990</b>

## Notes to the Financial Statements

### Industry sectors

The following table breaks down the Bank's credit exposures, at their carrying amounts, as categorised by the industry sectors of the Bank's counterparties

	Banks	Individuals	Real Estate	Manufacturing / Other	Total
	£	£	£	£	£
Balances with banks	4,625,746	-	-	-	4,625,746
Due from banks	71,412,705	-	-	-	71,412,705
Other financing	-	-	-	54,214	54,214
Murabaha financing	-	22,644	20,206,783	13,781,767	34,011,194
Wakala financing	-	-	-	-	-
Musharaka financing	-	-	14,725,326	-	14,725,326
Mudaraba financing	-	-	-	3,188,189	3,188,189
Ijara financing	-	-	-	485,187	485,187
Financial assets held to maturity	2,960,998	-	1,856,092	2,629,462	7,446,552
<b>31 December 2012</b>	<b>78,999,449</b>	<b>22,644</b>	<b>36,788,201</b>	<b>20,138,819</b>	<b>135,949,113</b>
Off-balance sheet					
Letters of credit	-	-	-	-	-
<b>31 December 2012</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Total</b>	<b>78,999,449</b>	<b>22,644</b>	<b>36,788,201</b>	<b>20,138,819</b>	<b>135,949,113</b>
Balances with banks	1,454,276	-	-	-	1,454,276
Due from banks	52,361,914	-	-	-	52,361,914
Other financing	-	-	-	91,088	91,088
Murabaha financing	-	51,735	17,210,328	5,966,495	23,228,558
Wakala financing	-	-	-	195,591	195,591
Musharaka financing	-	-	8,100,000	-	8,100,000
Mudaraba financing	-	-	-	3,781,755	3,781,755
Ijara financing	-	-	-	1,338,648	1,338,648
Financial assets held to maturity	4,210,887	-	-	-	4,210,887
<b>31 December 2011</b>	<b>58,027,077</b>	<b>51,735</b>	<b>25,310,328</b>	<b>11,373,577</b>	<b>94,762,717</b>
Off-balance sheet					
Letters of credit	316,273	-	-	-	316,273
<b>31 December 2011</b>	<b>316,273</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>316,273</b>
<b>Total</b>	<b>58,343,350</b>	<b>51,735</b>	<b>25,310,328</b>	<b>11,373,577</b>	<b>95,078,990</b>

## Notes to the Financial Statements

### *Credit quality*

The credit quality of the Bank's exposures is reviewed and managed by the RMC and EXCO

Credit quality is assessed using techniques which include information from the major External Credit Assessment Institutions ("ECAI") as well as specific financial data in order to determine internal risk ratings. The latter are mapped to the ECAI and Regulators' credit risk ratings.

The Bank has policies and procedures in place to monitor impairment events that could lead to losses in its asset portfolio. These policies and procedures cover specific loss events for individual significant exposures as well as events that relate to collective losses on groups of homogenous assets that have yet to be identified and assessed individually for impairment.

The Bank writes off a balance (and any related allowances for impairment) when the RMC determines that the balance is uncollectable. This determination would be reached after considering information such as the occurrence of significant changes in the obligor's financial position and an assessment of collateral levels.

During the year the Bank incurred impairment losses of £5,179,255 (2011: £113,605). The most significant of these was as a result of a UK retail operation that had been financed by the Bank in 2010 entering administration. This resulted in an impairment of £1,500,000 relating to equity options in the entities and 100% impairment provisions against outstanding financing of £3,377,957. Additionally, the provision against an exposure to a Middle Eastern corporate was increased from 80% to 100%, resulting in an additional impairment charge in the year of £301,298.

The table below shows past due amounts and impairments

	2012		2011	
	Due from banks	Financing arrangements	Due from banks	Financing arrangements
	£	£	£	£
Neither past due nor impaired	71,412,705	47,184,194	52,361,914	34,746,603
Individually impaired	-	5,279,916	-	1,989,037
Gross	<u>71,412,705</u>	<u>52,464,110</u>	<u>52,361,914</u>	<u>36,735,640</u>
Impairment	-	(5,279,916)	-	(1,600,661)
Total	<u>71,412,705</u>	<u>47,184,194</u>	<u>52,361,914</u>	<u>35,134,979</u>

The credit quality of the portfolio of financing arrangements and due from banks is further assessed by reference to the internal rating system adopted by the Bank. This is shown on the following page.



## Notes to the Financial Statements

	Investment Grade £	Standard Monitoring £	Special Monitoring £	Total £
Due from banks	55,494,162	15,918,543	-	71,412,705
Other financing	-	-	54,214	54,214
Murabaha financing	-	28,462,697	5,548,497	34,011,194
Wakala financing	-	-	-	-
Musharaka financing	14,725,326	-	-	14,725,326
Mudaraba financing	-	1,106,189	2,082,000	3,188,189
Ijara financing	128,645	356,542	-	485,187
Financial assets held to maturity	2,629,462	4,817,090	-	7,446,552
<b>31 December 2012</b>	<b>72,977,595</b>	<b>50,661,061</b>	<b>7,684,711</b>	<b>131,323,367</b>
Due from banks	52,361,914	-	-	52,361,914
Other financing	-	91,088	-	91,088
Murabaha financing	-	19,640,890	3,587,668	23,228,558
Wakala financing	-	195,591	-	195,591
Musharaka financing	-	8,100,000	-	8,100,000
Mudaraba financing	-	2,349,755	1,432,000	3,781,755
Ijara financing	-	1,338,648	-	1,338,648
Financial assets held to maturity	4,210,887	-	-	4,210,887
<b>31 December 2011</b>	<b>56,572,801</b>	<b>31,715,972</b>	<b>5,019,668</b>	<b>93,308,441</b>

As at 31 December 2012, the Bank has the following impaired assets for which it is undertaking special monitoring

- 1) UK retail corporates with total financing exposures of £3,377,957 (2011 £3,121,719) The total impairment provision against these assets as at 31 December is £3,377,957 (2011 £nil)
- 2) A Middle Eastern corporate with a total Murabaha financing amount due of £1,884,108 (2011 £1,884,108) A further impairment provision of £301,298 was raised in 2012 (2011 £111,753) The total impairment provision against this asset as at 31 December is £1,884,108 (2011 £1,582,810)
- 3) A UK individual with a total Murabaha financing amount due of £17,851 (2011 £17,851) The total impairment provision against this asset as at 31 December is £17,851 (2011 £17,851)

A full assessment of any other assets where a potential loss event has occurred has been completed and it has been concluded that no other impairment provision is required

## Notes to the Financial Statements

### Collateral

Where applicable, Risk Management assesses exposures against collateral coverage. This is completed as part of the initial credit assessment and then as part of periodic credit reviews. The fair value of collateral can vary monthly, annually or based on changes in circumstances or the market.

An analysis of collateral is shown in the following table, collateral is shown at the lower of the total exposure or the management estimation of the value of the collateral based on prevailing valuations.

	2012		2011	
	Exposure £	Collateral £	Exposure £	Collateral £
Balances with banks	4,625,746	-	1,454,276	-
Due from banks	71,412,705	-	52,361,914	-
Other financing	54,214	-	91,088	-
Murabaha financing	34,011,194	40,996,070	23,228,558	18,591,411
Wakala financing	-	-	195,591	-
Musharaka financing	14,725,326	16,470,136	8,100,000	8,100,000
Mudaraba financing	3,188,189	3,283,712	3,781,755	3,781,755
Ijara financing	485,187	150,000	1,338,648	1,050,000
Financial assets held to maturity	7,446,552	-	4,210,887	-
Letters of credit	-	-	316,273	-
Total credit risk	135,949,113	60,899,918	95,078,990	31,523,166

The Murabaha financing collateral of £40,996,070 is held against exposures totaling £25,919,106. Therefore, exposures totaling £8,092,088 have no collateral held against them, of which £3,543,704 represents the fully impaired exposures. With Musharaka financing, collateral is held against all exposures. The collateral held against Mudaraba financing covers exposures totaling £1,106,189 and £2,082,000 has no collateral held against it, of which £1,682,000 is fully impaired.

### Market risk

Market risk encompasses an adverse movement in the value of assets as a consequence of market movements such as rates, equity prices and commodity prices which are not matched by a corresponding movement in the value of liabilities.

The market risk within the Bank is managed in accordance with the FSA Capital Requirement Directive BIPRU 7 and includes all:

- trading book positions, and
- foreign exchange positions, whether or not in the trading book

The market risk definition can be further broken down into the sub-risk types shown on the following pages.

## Notes to the Financial Statements

### Exchange rate risk

The sensitivity of financial positions to adverse movements in foreign exchange rates. Exchange rate risk does not only arise as a result of direct foreign exchange dealings, but can also result from foreign currency based transactions such as financing, deposits, Islamic derivative trades or through foreign currency commission payments and receipts. The following table summarises the Bank's exposures arising from its financial instruments.

	USD £	EUR £	GBP £	QAR £	Other £	Total £
<b>Assets</b>						
Cash and balances with banks	436,235	273,348	3,863,626	8,574	44,462	4,626,245
Due from banks	45,010,209	3,222,648	23,179,848	-	-	71,412,705
Financing arrangements	7,452,522	-	45,011,588	-	-	52,464,110
Financial assets held for trading	25,827,202	-	-	-	-	25,827,202
Financial assets held to maturity	4,485,554	-	2,960,998	-	-	7,446,552
Financial assets available for sale	2,036,751	-	2,206,242	-	-	4,242,993
Derivative financial instruments	-	-	(309)	-	-	(309)
<b>31 December 2012</b>	<b>85,248,473</b>	<b>3,495,996</b>	<b>77,221,993</b>	<b>8,574</b>	<b>44,462</b>	<b>166,019,498</b>
<b>Liabilities</b>						
Due to banks	4,641,316	48,015	38,839,192	-	-	43,528,523
Due to customers	90,056,615	3,296,076	9,466,672	-	-	102,819,363
Loan from related party	-	-	-	-	-	-
Subordinated Loan	-	-	4,757,834	-	-	4,757,834
<b>31 December 2012</b>	<b>94,697,931</b>	<b>3,344,091</b>	<b>53,063,698</b>	<b>-</b>	<b>-</b>	<b>151,105,720</b>
<b>Net on balance sheet financial position</b>	<b>(9,449,458)</b>	<b>151,905</b>	<b>24,158,295</b>	<b>8,574</b>	<b>44,462</b>	<b>14,913,778</b>
Forward foreign exchange contracts	14,281,721	(1,599,951)	-	-	-	12,681,770

## Notes to the Financial Statements

	USD £	EUR £	GBP £	QAR £	Other £	Total £
<b>Assets</b>						
Cash and balances with banks	33,104	34,426	1,336,994	166	50,403	1,455,093
Due from banks	25,179,623	5,442,291	21,740,000	-	-	52,361,914
Financing arrangements	2,846,432	-	33,889,208	-	-	36,735,640
Financial assets held for trading	27,006,222	-	-	-	-	27,006,222
Financial assets held to maturity	4,210,887	-	-	-	-	4,210,887
Financial assets available for sale	-	-	1,900,693	-	-	1,900,693
Derivative financial instruments	-	-	2,324,368	-	-	2,324,368
31 December 2011	59,276,268	5,476,717	61,191,263	166	50,403	125,994,817
<b>Liabilities</b>						
Due to banks	7,266,419	2,110,488	16,524,642	-	-	25,901,549
Due to customers	74,835,954	3,349,102	2,934,830	-	-	81,119,886
Loan from related party	-	-	4,757,834	-	-	4,757,834
31 December 2011	82,102,373	5,459,590	24,217,306	-	-	111,779,269
Net on balance sheet financial position	(22,826,105)	17,127	36,973,957	166	50,403	14,215,548
Forward foreign exchange contract	22,600,000	-	-	-	-	22,600,000

## Notes to the Financial Statements

The Bank has a policy of matching foreign currency assets and liabilities and as at 31 December 2012, held a net exposure to exchange rate risk equivalent to £3,437,253 (2011 £158,409)

### ***Commodity risk***

The sensitivity of financial positions to adverse movements in commodity market dynamics. Movements may typically include changes in commodity prices, commodity price volatility and the price relationship between different commodities or commodity indices (correlation). As at 31 December 2012, the Bank had no direct exposure to commodity risk (2011 £nil)

### ***Equity risk***

The sensitivity of financial positions to adverse movements in stock market dynamics. Movements may typically include changes in equity prices, equity price volatility, price relationship between different equities or indices (correlation) and dividend payments. The Bank has been granted Wa'ads relating to the shares of four UK based corporates. As at 31 December 2012, the Bank's total equity exposure, relating to these Wa'ads, was £4,242,993 (2011 £3,400,609)

### ***Profit rate risk (trading book only)***

The sensitivity of financial positions to adverse movements in profit rates. The risk is largely the result of the mismatching of assets and liabilities with respect to the maturity and re-pricing profiles, as well as the differing amounts by which rates may move across various tenors of the yield curve.

The Bank's profit rate risk sensitivity analysis considers a number of factors such as historical data and stress testing based scenarios, this analysis also includes net present value of cash flows based on respective currency yield curves in which trading book portfolio instruments are denominated.

The profit rate risk of the trading book portfolio is reviewed on daily basis. If the risk related to any instrument in the portfolio exceeds the tolerance limits set by the RMC, it will be disposed of from the portfolio.

As at 31 December 2012, the Bank had £1,299,227 exposure to profit rate risk in the trading book (2011 £1,231,957)

### ***Operational risk***

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Bank's processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks.

The Bank's objective in managing operational risk is to implement an integrated internal control and operating infrastructure that supports process efficiency and customer needs, whilst effectively reducing the risk of error and financial loss in a cost effective manner. The overall operational risk framework is set by the Board of Directors and is documented within the Bank's Operational Risk Policy under the guidance of the RMC.

## Notes to the Financial Statements

Operational risk management is considered to be the responsibility of all staff. The following outlines the governance structure for the Bank's operational risk framework:

- the Board of Directors approves the strategy and policy documents
- the following operational risk factors are monitored by the RMC, high risk areas as defined by departmental risk self-assessments, organisational deficiencies, inadequate policies and procedures, key risk indicators, and loss information
- a detailed monthly report of all operational activities is made available to senior management and the RMC

The Compliance team is responsible for ensuring that all aspects of regulatory risk impacting the Bank are appropriately reviewed and managed. The Bank does not currently have a dedicated in-house legal function but utilises professional legal firms for all matters requiring legal advice, and this is overseen by the EXCO.

The Audit and Risk Committee and Board are currently in the process of assessing and implementing the optimum solution for internal audit. Reports from Internal Audit are reviewed by the Audit and Risk Committee which is also responsible for reviewing and approving the annual internal audit plan.

### Shari'a compliance risk

Shari'a compliance risk is the risk of loss arising from non-compliance of products or services offered by the Bank with Shari'a principles. The Bank has a Shari'a Supervisory Committee (SSC) which is responsible for overseeing that all products and activities of the Bank are Shari'a compliant. The members of the SSC are leading experts in the interpretation of Islamic law and its applications in the contemporary financial markets. The SSC meets on a regular basis to review all contracts and agreements relating to the Bank's business and all products and services are only offered once certified by the SSC.

### Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations due from its financial liabilities. The risk is managed by ensuring that the Bank always has sufficient liquidity to meet its liabilities when due. The Bank's Treasury department is responsible for formulating an overall market strategy for managing liquidity which is then approved by ALCO. The Treasury department monitors the liquidity profile of all financial assets and liabilities, including projected cash flows from current and future business, and this is reviewed by Risk Management and reported to members of ALCO on a daily basis.

Residual contractual maturities of the Bank's portfolio is managed using 'Gap analysis' methodology and measures exposures up to six months. A daily report reflecting sight to six months is distributed to the Treasury, Finance and Operations departments and to the EXCO.

Details of the Company's net liquid assets are summarised in the table on the following page by the maturity profile of the Company's assets and liabilities based on the contractual repayment arrangements. The contractual maturities of assets and liabilities have been determined on the basis of the remaining period at the balance sheet date to the contractual maturity date. Financial assets held for trading can be realised immediately in the open market. The maturity profile is monitored by management to ensure adequate liquidity is maintained.

## Notes to the Financial Statements

	Up to 1 month	1-3 months	3-12 months	1-5 years	More than 5 years	Total
<b>31 December 2012</b>						
<b>Assets</b>						
Cash and balances with banks	4,626,245	-	-	-	-	4,626,245
Due from banks	43,579,878	13,198,122	250,000	14,384,705	-	71,412,705
Financing arrangements	-	-	5,744,043	41,440,150	5,279,917	52,464,110
Financial assets held for trading	19,444,105	-	6,383,097	-	-	25,827,202
Financial assets held to maturity	-	-	-	7,446,552	-	7,446,552
Financial assets available for sale	2,017,402	-	-	2,225,591	-	4,242,993
Derivative financial instruments	(152)	(157)	-	-	-	(309)
<b>Total assets</b>	<b>69,667,478</b>	<b>13,197,965</b>	<b>12,377,140</b>	<b>65,496,998</b>	<b>5,279,917</b>	<b>166,019,498</b>
<b>Liabilities</b>						
Due to banks	21,247,127	12,868,715	5,912,681	3,500,000	-	43,528,523
Due to customers	10,010,428	6,231,735	37,111,682	49,465,518	-	102,819,363
Loan from related party	-	-	-	-	-	-
Subordinated loan	-	-	-	4,757,834	-	4,757,834
<b>Total liabilities</b>	<b>31,257,555</b>	<b>19,100,450</b>	<b>43,024,363</b>	<b>57,723,352</b>	<b>-</b>	<b>151,105,720</b>
<b>Difference</b>	<b>38,409,923</b>	<b>(5,902,485)</b>	<b>(30,647,223)</b>	<b>7,773,646</b>	<b>5,279,917</b>	<b>14,913,778</b>
<b>31 December 2011</b>						
<b>Assets</b>						
Cash and balances with banks	1,455,093	-	-	-	-	1,455,093
Due from banks	37,312,396	-	-	15,049,518	-	52,361,914
Financing arrangements	2,184,628	1,949,755	6,710,813	25,890,444	-	36,735,640
Financial assets held for trading	4,374,184	-	-	13,057,894	9,574,144	27,006,222
Financial assets held to maturity	-	-	-	4,210,887	-	4,210,887
Financial assets available for sale	1,900,693	-	-	-	-	1,900,693
Derivative financial instruments	2,324,368	-	-	-	-	2,324,368
<b>Total assets</b>	<b>49,551,362</b>	<b>1,949,755</b>	<b>6,710,813</b>	<b>58,208,743</b>	<b>9,574,144</b>	<b>125,994,817</b>
<b>Liabilities</b>						
Due to banks	14,085,897	973,526	10,842,126	-	-	25,901,549
Due to customers	15,519,982	15,164,339	2,265,519	48,170,046	-	81,119,886
Loan from related party	-	-	-	-	4,757,834	4,757,834
<b>Total liabilities</b>	<b>29,605,879</b>	<b>16,137,865</b>	<b>13,107,645</b>	<b>48,170,046</b>	<b>4,757,834</b>	<b>111,779,269</b>
<b>Difference</b>	<b>19,945,483</b>	<b>(14,188,110)</b>	<b>(6,396,832)</b>	<b>10,038,697</b>	<b>4,816,310</b>	<b>14,215,548</b>

## Notes to the Financial Statements

### Profit rate risk

This risk arises from the effects of changes in profit rates on the re-pricing of assets and liabilities, and covers both fixed and variable profit rates. The Bank manages such risks through the use of Gap analysis and an economic value methodology using the profit rate sensitivity to changes in 1 month LIBOR rates.

The profit rate sensitivity is measured and monitored against revenue and capital on a daily basis in the Risk Management report which is distributed to the Treasury department and ALCO. A detailed report is distributed monthly to EXCO and the Board of Directors.

The profit rate sensitivity is shown in the table below:

	2012	2011
Net income from financing activities	£3,852,014	£1,864,728
Parallel rate shock risk		
- 1% rate shock	£407,327	£441,797
Impact of rate shock on capital		
- 1% rate increase	2.87%	2.57%
- 1% rate decrease	-2.87%	-2.57%
Impact of rate shock on net income		
- 1% rate increase	11%	24%
- 1% rate decrease	-11%	-24%

### 29 Fair value of financial assets and liabilities

In the opinion of the Directors, the fair value of financial assets and financial liabilities are not materially different from their carrying value.

#### *Fair value hierarchy*

IFRS 7 specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources, unobservable inputs reflect the Company's market assumptions. These two types of inputs have created the following fair value hierarchy:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities. This level includes listed equity securities on exchanges.
- Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices).
- Level 3 – Inputs for the asset or liability that are not based on observable market data (unobservable inputs). This level includes equity investments with significant unobservable components.



## Notes to the Financial Statements

This hierarchy requires the use of observable market data when available. The Company considers relevant and observable market prices in its valuations where possible.

The fair value for investments in Sukuk and funds under 'financial assets held for trading' are based on quoted prices as defined in level 1 under IFRS 7. The fair value of investments in structured notes is based on observable market prices as defined in level 2 under IFRS 7. The fair value of the equity Wa'ads, included within financial assets available for sale and derivative financial instruments are based on independent valuations of the underlying business to which the Wa'ad relates. These valuations incorporate all available information about the business including a review of its order book, an estimate of future cash flows and related market data, and are within level 3 of the fair value hierarchy under IFRS 7.

The following table presents the Bank's assets that are measured at fair value as at 31 December

31 December 2012	Level 1 £	Level 2 £	Level 3 £	Total £
Financial assets at fair value through profit and loss				
- Debt instruments	18,944,121	6,383,097	-	25,327,218
- Equity instruments	499,984	-	-	499,984
Derivative financial instruments	-	(309)	-	(309)
Financial assets available for sale				
- Equity instruments	-	-	4,242,993	4,242,993
<b>Total Assets</b>	<b>19,444,105</b>	<b>6,382,788</b>	<b>4,242,993</b>	<b>30,069,886</b>

### 31 December 2011

Financial assets at fair value through profit and loss

- Debt instruments	23,258,277	3,261,700	-	26,519,977
- Equity instruments	486,245	-	-	486,245
Derivative financial instruments	-	824,368	1,500,000	2,324,368
Financial assets available for sale				
- Equity interests	-	1,900,693	-	1,900,693
<b>Total Assets</b>	<b>23,744,522</b>	<b>5,986,761</b>	<b>1,500,000</b>	<b>31,231,283</b>

## Notes to the Financial Statements

The following table presents the changes in level 3 instruments

	Financial assets available for sale £	Derivative financial instruments £	Total £
Balance as at 1 January 2012	-	1,500,000	1,500,000
Transfers into level 3 instruments	1,900,693	-	1,900,693
Level 3 instruments recognised in year	2,036,751	-	2,036,751
Gain / (loss) on level 3 instruments	305,549	(1,500,000)	(1,194,451)
<b>Balance as at 31 December 2012</b>	<b>4,242,993</b>	<b>-</b>	<b>4,242,993</b>
Balance as at 1 January 2011	-	-	-
Level 3 instruments recognised in year	-	1,500,000	1,500,000
<b>Balance as at 31 December 2011</b>	<b>-</b>	<b>1,500,000</b>	<b>1,500,000</b>

Financial assets available for sale include equity interests (in the form Wa'ads) in three counterparties, where independent professional valuations were completed to obtain the fair value as at 31 December 2012

- 1) In a technology and media company The value of the Wa'ad as at 31 December 2012 was £2,017,402 (2011 £1,900,693)
- 2) In a pharmaceutical research company The value of the Wa'ad as at 31 December 2012 was £188,840 (2011 £nil)
- 3) In a specialist financial structuring company This Wa'ad was recognised during the current year and was valued at £2,036,751

As noted above, all three Wa'ads were independently valued as at 31 December 2012. The valuation of the Wa'ad in the financial structuring company was inherently more complex, given the nature of the company's business, whereby actual and projected income is based on a relatively small number of large contracts. Additional work was completed to assess the current project pipeline to ensure that the valuation appeared reasonable.

Profit for the year would increase/decrease by £221,150, as a result of a 5% change in the fair value of financial assets available for sale, all of which are within level 3.

### 30 Events after the balance sheet date

There were no events between the balance sheet date and the date when the financial statements were signed, which would have had any material impact on the financial results for the year ended 31 December 2012.