FUND FOR LOCAL AUTHORITIES AND GOVERNMENTS IN BULGARIA – FLAG JSC

ANNUAL ACTIVITIES REPORT AND FINANCIAL STATEMENTS
31 December, 2010

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FUND FOR LOCAL AUTHORITIES AND GOVERNMENTS IN BULGARIA – FLAG JSC

Background Information

Board of Directors:

Ekaterina Spasova Gecheva – Zaharieva - Chairperson
Ivelina Vesselinova Vassileva – Deputy Chairperson
Emil Rumenov Savov - member
Daniel Bryan Berg - member
Lilyana Pavlova Nikolova - member
Vessela Danailova Daneva - member
Yulia Petkova Tsolova –Ilieva - member

Registered address

Sofia, 17-19 Sv. Sv. Kiril I Metodi St.

Management address

Sofia 27 Solunska St.

Legal advisor

Dessislava Ivanova-Atanassova

Servicing banks

UniCredit Bulbank
Reiffaisenbank
Piraeus Bank

Auditor

Earns & Young Audit Ltd.
Business Park Sofia
Building 10, floor 2
Mladost 4
Sofia 1766

ACTIVITIES REPORT

For the year ending on 31 December 2010

ANNUAL REPORT

On the Activity of
Fund for Local Authorities and Governments in Bulgaria – FLAG JSC
for FY 2010

This Report was drawn up in compliance with the requirements of article 23 of the Regulation on the Way the State shall exercise its rights in commercial entities with state interest in owner's equity and in compliance with the Commerce Act.

1. Business Programme

1.1. Equity and Loan Resource

The share capital of the company stands at BGN 60 million, paid in three installments in 2008 and 2009. Thus, together with the long-term credit resource of EURO 35 million borrowed in 2010, FLAG has a loan resource of BGN 129.1 million.

1.2. Management

The Fund is managed by the Board of Directors (BD), consisting of seven members. The BD organizes and manages the current activities of the Fund in delivering all its functions. The BD held 15 meetings in 2010.

The following changes in the composition of the Fund were executed in the period under review, upon decision of the sole proprietor of the Fund:

- ✓ James Hyslop filed in September his resignation request as member of the BD and Daniel Berg was appointed to the BD as representative of the European Bank for Reconstruction and Development (EBRD) in November. This fact was recorded in the Commercial register in 2011.

- ✓ On 7 September the sole Proprietor made changes in the structure of the BD, replacing the representative of the Ministry of Agriculture and Food with a representative of the Ministry of Finance (Ministry of Finance) – Yulia Tsolova replaced Preslav Borissov as a member of the BD.

At the end of 2010 the Board of Directors consisted of the following members: Ekaterina Zaharieva (MRDPW) – Chairperson, Ivelina Vassileva (MEW) – Deputy Chairperson, Lilyana Pavlova (NRDPW) – member, Vessela Daneva (MoF) – member, Yulia Tsolova (MoF) – member, James Hyslop (EBRD) – member and Emil Savov (National Association of Municipalities in the RP) – member and Executive Director.

The Bulgarian legislation requires from the management to prepare financial statements for every financial year, giving a true and fair view of the financial condition of the company as at the year-end, its financial disclosure and cash flows.

The management acknowledges that it has been consistently applying adequate accounting policies in preparing the annual financial statements as at 31 December, 2010 and has come up with reasonable and prudent judgments, assumptions and estimates.

The management also acknowledges that it has applied the existing accounting standards and has observed the going concern principle when drawing up the financial statements.

The management is responsible for the proper management of the accounting ledgers, for the expedient asset management and adoption of the steps necessary to avoid and reveal any possible fraud or other irregularities.

1.3. Human Resources

The Fund's staff possessed the appropriate qualifications to perform the lending activities in 2010. The structure and number of staff are presented in the table below.

Position	Number at the end of 2010
Experts at Projects and Monitoring Directorate	2
Experts at Finance and Risk Management Directorate	1
Experts at Lending Directorate	3
Director of Projects and Monitoring Directorate	1
Director of Lending Directorate	1
Internal auditor	1
Office manager	1
Total	**10**

The accounting and legal servicing, as well as the maintenance of the computer network have been contracted out to external suppliers.

1.4. External Auditor for 2010

At a meeting on 22 October, 2010 the Board of Directors approved the outcome of a public procurement procedure for selection of an external auditor for 2010 pursuant to article 2, para 1 p. 2 of the Regulation on Awarding Small Public Procurement and approved Earns & Young Audit Ltd. as contractor. This decision was later approved by the sole proprietor of the Fund.

1.5. Loan Agreement with EBRD

The last, 14th disbursement under the First Loan Agreement with EBRD was received in April, 2010, with which the loan of EURO 35 million was fully absorbed. The funds under the Second Loan Agreement, signed on 3 July, 2009, have not been disbursed in 2010.

1.6. Main Results of the Lending Activity in 2010

56 loans were extended to 46 municipalities in 2010, amounting to BGN 62.8 million, supporting the implementation of projects in the amount of BGN 145 million, where the average share of the loan within the budget of the respective project was 42%. The typical loan extended to a municipality was one for bridge financing in the amount of BGN 1.06 million, with maturity of 15 months. FLAG covered two new programmes this year: The Rural Areas Development Programme (RADP) and the Financial Facility of the EEA (FF EEA).

The table below presents the loans approved in 2009 and 2010 by type and principal repayment source.

FUND FOR LOCAL AUTHORITIES AND GOVERNMENTS IN BULGARIA – FLAG JSC

ACTIVITIES REPORT

For the year ending on 31 December 2010

Types of loans	Number of loans for 2009	Value of loans approved in 2009 *(in BGN)*	Number of loans for 2010	Value of loans approved in 2010 *(in BGN)*
Long-term loans	**12**	**13,748,498**	**13**	**17,043,122**
incl. bridge financing	11	12,969,898	9	14,687,438
incl. with own funds	1	778,600	4	2,355,684
Short-term loans	**57**	**58,018,052**	**43**	**45,742,136**
incl. bridge financing	56	57,867,261	43	45,742,136
incl. with own funds	1	150,791	0	0
Total	**69**	**71,766,550**	**56**	**62,785,258**

The three tables that follow present the typology of the lending activity in 2010 by types of projects, by OPs and by sources for repayment of principals.

By type of loans	Number of loans	Total value in BGN	Value in BGN			Maturity in months		
			Min.	Max.	Average	Min.	Max.	Average
Investment loans	46	60,797,242	77,455	5,044,693	1,321,679	5	67	13
Preparation with TA	10	1,988,016	112,000	310,000	198,802	6	36	14

По оперативни програми	Number of loans	Total value in BGN	Value in BGN			Maturity in months		
			Min.	Max.	Min.	Max.	Min.	Max.
Regional development	36	48,880,939	160,000	3,800,000	1,357,804	4	67	12
Environment	13	11,991,650	112,000	5,044,693	922,435	6	36	14
FF EEA	5	1,487,669	122,680	464,989	297,534	7	60	20
RADP	2	425,000	77,455	347,545	212,500	7	8	8

By repayment source	Number of loans	Total value in BGN	Value in BGN			Maturity in months		
			Min.	Max.	Min.	Max.	Min.	Max.
Operational Programmes	52	60,429,574	77,455	5,044,693	1,162,107	4	24	10
Own funds	4	2,355,684	122,680	1,576,573	588,921	36	67	51

The funds absorbed in 2010 under signed loan contracts amount to BGN 64.12 million (BGN 65.7 million in 2009) , and the repaid loans stand at BGN 64.9 million (against BGN 17.3 million in 2009).

The year 2010 saw the signing of 116 annexes to 68 loan contracts, referring mainly to the repayment schedule.

Two of the loan applications filed in 2010 for a total amount of BGN 1.8 million are being considered now.

40 loans, in the amount of BGN 39.5 million were repaid in full in 2010.

As at the end of 2010 the municipalities Karlovo, Momchilgrad, Lom, Nikola Kozlevo, Dragoman and Sopot were in arrears of 7 or more days.

Two of the filed loan applications were not approved, and one application was approved, but the municipality declared that it was not going to use the loan before signing the contract.

1.7. Changes in the Lending Policy

In December the Board of Directors changes the terms and conditions for loans extended for implementation of technical assistance projects, which are part of an overall investment project, by eliminating the limitations regarding the size of the loan and its servicing. The changes are in line with the new policy of OPE for direct extension of grants to specified beneficiaries. The municipalities may thus finance the designing in a way identical with the investment part.

1.8. Information and Publicity

It has become a tradition for representatives of the Fund to participate in the major events of the municipalities, organized by the National Association of municipalities in RB where the opportunities offered by the Fund are presented and the municipalities are given specific consultations.
The information on the Internet site of FLAG is regularly updated and maintained. An information material was also published in 2010, reflecting the lending activities of the Fund from the time of its establishment till October, 2010.

2. Financial Condition

2.1. Report and Structure of Income and Expenses

2.1.1. Statement of Income and Expenses

EXPENSES, BGN thous.		**3,623**
1	Remun. BD, Excec. Director and social security contributions	69
2	Rental office and consumables	72
3	Accounting services	21
4	Auditor services	32
5	Notary fees, legal services, courier services, notices, IT maintenance, insurance, translations	26
6	Other current expenses	12
7	Communication services	8
8	Stationery	18
9	Other materials	6
10	Fuel and automobile materials	3
11	Depreciation	18
12	Salaries and social insurance contributions	256
13	Business trips	1
14	EBRD costs-non-financial	75
15	Bank fees	525
16	Expenses on interest charged on EBRD loan – charged and not paid as at 31 December 2010	975
17	Expenses on interest charged on EBRD loan – charged and paid in 2010	1,314
18	Expenses on impairment	143
19.	Expenses on forex transactions	49
INCOME ITEMS, BGN thous.		**8,961**
1	Income from interest on loans	3,037
2	Income from default interest on loans	28
3	Income from fees on loans	26
4	Income from interest on deposits, charged but not received in 2010	2,007
5	Income from interest on deposits, charged and received in 2010	3,863
DEPOSITS, BGN thous.		**85,036**
1	Raiffeisenbank	45,134
2	UniCredit	27,902

3	Piraeus	12,000

2.1.2. Structure of Expenses

Groups of expenses	Amount, BGN thous.	Share of total expenses
Operational costs	117	3.23%
Hired services	80	2.21%
Acquisition of LTTA and depreciation	18	0.5%
Remuneration – staff, BD	326	9.0%
UniCredit Management fee, other fees	9	0.25%
On EBRD loans - interest	2,289	63.17%
On EBRD loans – fees	432	11.92%
On EBRD loans – other expenses	160	4.42%
Impairment/provisions	143	3.95%
Expenses on forex transactions	49	1.35%
	3,623	

2.1.3. Income

The total income of the Fund for the period stands at BGN 8,961 thous., broken down by type in the table below:

Income	2010	Share
Interest and fees on loans and other income (BGN thous.)	3,091	34%
Yield from deposits (BGN thous.)	5,870	66%
Total	**8,961**	

- **2.1.3.1. From extended loans** – at average interest rate of 5.431% the yield, including interest and commitment fee, is in the amount of BGN 3,065 thous. The average interest reflects the surcharge for FLAG reduced in September from 2.25 % to 1.715 %. The real interest burden for the municipalities, given the compensation received pursuant to CoM Decree 205/2010, is 2.314%.

- **2.1.3.2. From management of temporarily unemployed funds** – FLAG has concluded three contracts with banks for deposits with overall yield of BGN 5.87 million, distributed among the different sources like follows:

Source	Paid in 2010 (BGN thous.)	Due as at 31.12.2010 (BGN thous.)	Total (BGN thous.)
Raiffeisenbank	3,298	100	3,398
UniCredit	564	946	1,511
Piraeus	-	961	961
Total:	**3,863**	**2,007**	**5,870**

2.2 Results for the current period

The profit of the Fund before taxes amounts to BGN 5,338 thous., and the net profit – BGN 4,805 thous.

2.3 Dividends and distribution of profit

The Company forms a “Reserve” fund in the amount of 10% of the net profit – BGN 480 thous., after which a dividend is distributed to the state in the amount of BGN 3,460 thous.

2.4 Investment

As at 31 December 2010 FLAG JSC has no equity participation in other companies.

3. Most likely development of the Company in 2011

The Business Plan was prepared on the basis of the following:

- ✓ The loan contracts concluded in 2010, the servicing of which will continue in 2011;
- ✓ Expected parameters of loan applications which are being processed now;
- ✓ Indicative lists and repayment schedules of OPRD and OPE, information about RADP and EEA, meetings with representatives of the Managing Authority of OPE and of OPRD, talks with municipalities;
- ✓ A set of assumptions, based on FLAG's experience from 2009 - 2010.

3.1 Overall Estimate of Demanded Loan Resource

The summarized estimate of the expected new loan resources is presented in the table below in BGN million:

Programmes/type of loans	Bridge financing	Municipal co-financing	Total
OPRD	51.3	2.1	53.4
OPE	14.8	17.3	32.1
RADP	16.3	-	16.3
EEA	1.4	-	1.4
TBC	3.4	0.1	3.5
Total:	**87.2**	**19.5**	**106.7**

3.2 Financial Proceeds and Result

The total amount of financial proceeds from the activity is projected to come to BGN 6.2 million, where 56% will be revenues from loans extended to the municipalities.

3.3 Information as per article 187e and article 247 of the Commerce Act

Own shares have not been acquired and transferred in 2010.

3.4 Branches of the Enterprise

The Company has no branches.

Prepared by: Emil Savov – Executive Director
March 2011

Report of the Independent Auditor

To the Sole Proprietor

Of Fund for Local Authorities and Governments in Bulgaria – FLAG JSCHa

Report on the Financial Statements

We have performed an audit of the accompanying financial statements of Fund for Local Authorities and Governments in Bulgaria – FLAG JSC, which comprise the report on the financial condition as at 31 December, 2010, the consolidated Income Statement, Statement of Changes in Owner's Equity and Cash Flow Statement for the year ending on this date, as well as the summary of significant accounting policies and other explanatory notes.

Management Responsibility for the Financial Statements

Management is responsible for the preparation and presentation of these financial statements, which give a true and fair picture, in accordance with the International Financial Reporting Standards, the way they are accepted and applied in the European Union as well as for putting in place such an internal control system as the management deems necessary for the preparation of financial statements that are free from material misstatement, whether due to error or fraud.

Auditor's responsibility

Our responsibility is confined to expressing an auditor opinion on these financial statements, based on the audit we have conducted. This audit was performed in compliance with the International Auditing Standards. These standards require that we comply with the ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

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

We believe that the audit provides a sufficient and appropriate basis for our audit opinion.

Opinion

In our opinion the financial statements give a true and fair view of the financial position of Fund for Local Authorities and Governments in Bulgaria - FLAG JSC as of 31 December 2009, as well as of its financial performance and its cash flows for the year then ended in conformity with the International Financial Reporting Standards, as they are accepted and applied in the European Union.

Other Issues

The financial statements of Fund for Local Authorities and Governments in Bulgaria – FLAG JSC for the year ending on 31 December 2009 are audited by another auditor who has expressed a non modified opinion on these statements on 24 March, 2010.

Report on other Legal and Regulatory Requirements

In accordance with article 38, para 4 of the Accountancy Act we have familiarized ourselves with the content of the accompanying Activities Report for 2010. In our opinion the Activities Report presented by the management is consistent with the financial statements for the year ending on 31 December, 2010.

Joanis Mistakidis

Manager

„Earnst and Young Audit Ltd.

Nikolai Garnev, FCCA, CPA

Registered auditor

25 March 2011

Sofia, Bulgaria

FUND FOR LOCAL AUTHORITIES AND GOVERNMENTS IN BULGARIA – FLAG JSC
COMPREHENSIVE INCOME STATEMENT

For the year ending on 31 December 2010

	Notes	2010	2009
		BGN thous.	*BGN thous.*
Interest income	5.1	8,935	4,785
Costs on interest and fees	5.2	(2,863)	(979)
Other income from activity, net		26	28
Total operational income		**6,098**	**3,834**
Costs on impairment of extended loans	11	(143)	-
Labour costs	5.3	(326)	(319)
Depreciation costs	9	(18)	(19)
Other operational costs	5.4	(273)	(361)
Profit before tax		**5,338**	**3,135**
Costs on income taxes	6	(533)	(313)
Profit for the year		**4,805**	**2,822**
Other comprehensive income for the year, net of taxes		-	-
Total comprehensive income for the year, net of taxes		**4,805**	**2,822**

Emil Rumenov Savov
Executive Director

Kalinka Ruskova Todorova
Chief accountant

The Financial Statements were approved for issuing by virtue of decision of the Board of Directors dated 22 March, 2011

The explanatory notes from p.7 to p. 30 constitute an inseparable part of the Financial Statements.

FUND FOR LOCAL AUTHORITIES AND GOVERNMENTS IN BULGARIA – FLAG JSC
BALANCE-SHEET

For the year ending on 31 December 2010

	Notes	2010	2009
		BGN thous.	*BGN thous.*
ASSETS			
Cash and cash equivalents	7	87,089	66,489
Receivables and prepaid expenses	8	7	5
Extended loans	11	47,545	48,508
Assets on deferred taxes	10	1	1
Plant and Equipment	9	25	42
Prepaid initial costs for fees under EBRD loan	12, 18	660	722
TOTAL ASSETS		**135,327**	**115,767**
LIABILITIES AND EQUITY			
Liabilities			
Liabilities to staff and social insurance liabilities	13	49	57
Tax liabilities	14	209	253
Other liabilities		9	8
Liabilities under EBRD loan	12	69,133	52,296
Total liabilities		**69,400**	**52,614**
Equity			
Authorized capital	15.1	60,000	60,000
Statutory reserves	15.2	342	60
Retained earnings		5,585	3,093
Total equity		**65,927**	**63,153**
TOTAL LIABILITIES AND EQUITY		**135,327**	**115,767**

Emil Rumenov Savov
Executive Director

Kalinka Ruskova Todorova
Chief accountant

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FUND FOR LOCAL AUTHORITIES AND GOVERNMENTS IN BULGARIA – FLAG JSC
STATEMENT OF CHANGES IN EQUITY

For the year ending on 31 December 2010

	Authorized capital (Note 15.1)	Retained earnings	Statutory reserves (Note 15.2)	Total
	BGN thous.	*BGN thous.*	*BGN thous.*	*BGN thous.*
Balance as of 1 January 2009	**30,000**	**602**	**-**	**30,602**
Profit for the year	-	2,822	-	2,822
Other comprehensive income	-	-	-	-
Total comprehensive income	-	2,822	-	2,822
Increase of authorized capital	30,000	-	-	30,000
Distribution of dividends (Note 17)	-	(271)	-	(271)
Transfer of reserves	-	(60)	60	-
As at 31 December 2009	**60,000**	**3,093**	**60**	**63,153**
Balance as of 1 January 2010	**60,000**	**3,093**	**60**	**63,153**
Profit for the year	-	4,805	-	4,805
Other comprehensive income	-	-	-	-
Total comprehensive income	-	4,805	-	4,805
Distribution of dividends (Note 17)	-	(2,031)	-	(2,031)
Transfer of reserves	-	(282)	282	-
As at 31 December 2010	**60,000**	**5,585**	**342**	**65,927**

Emil Rumenov Savov
Executive Director

Kalinka Ruskova Todorova
Chief accountant

The Financial Statements were approved for issuing by virtue of decision of the Board of Directors dated 22 March, 2011

The explanatory notes from p.7 to p. 30 constitute an inseparable part of the Financial Statements.

FUND FOR LOCAL AUTHORITIES AND GOVERNMENTS IN BULGARIA – FLAG JSC
CASHFLOW STATEMENT

For the year ending on 31 December 2010

	Notes	2010	2009
		хил. лв.	*хил. лв.*
Cash flow from operational activity			
Interest received on bank deposits		5,869	3,570
Loans extended to municipalities		(64,116)	(65,744)
Loans repaid by municipalities		64,944	17,283
Interest received on extended loans		3,082	1,197
Payments to suppliers		(266)	(342)
Payments to staff and for social insurance		(317)	(286)
Other proceeds / (payments), net		(28)	(1)
Paid income tax	14	(577)	(132)
Net cash flow from (used in) operational activities		**8,591**	**(44,455)**
Cash flow from investment activities			
Purchase of equipment and other long-term assets		(1)	(4)
Net cash flow used in investment activity		**(1)**	**(4)**
Cash flow from financial activity			
EBRD loan		16,344	51,984
Paid dividends	17	(2,031)	(271)
Contributions to authorized capital		-	30,000
Paid interest on EBRD loans		(2,303)	(1,385)
Net cash flow from financial activity		**12,010**	**80,328**
Net increase of cash and cash equivalents		**20,600**	**35,869**
Cash and cash equivalents, beginning of period	7	66,489	30,620
Cash and cash equivalents, end of period	7	**87,089**	**66,489**

Emil Rumenov Savov
Executive Director

Kalinka Ruskova Todorova
Chief accountant

The Financial Statements were approved for issuing by virtue of decision of the Board of Directors dated 22 March, 2011

The explanatory notes from p.7 to p. 30 constitute an inseparable part of the Financial Statements.

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1. Corporate information

The financial statements of FLAGB FLAG EAD (the Company) for the year ended 31 December 2010 was prepared on 10 March 2011 and was approved for issue by virtue of decision of the Board of Directors dated 22 March 2011.

FLAGB FLAG EAD is a joint-stock company incorporated by virtue of Decision No 1 / 04.07.2007 under company file 10151/2007 of Sofia City Court, having its seat in Sofia, Bulgaria. The financial year of the Company ends on 31 December.

The core activity of the Company includes financing against consideration of the municipal infrastructure and other projects and co-financing for the development and implementation of projects of the European Union.

As at 31 December 2010 the shareholders of the Company include:
the Republic of Bulgaria represented by the Minister of Regional Development and Public Works - 100.00 %

2.1 Basis of preparation

The accompanying financial statements have been prepared under the historical cost convention.

The financial statements have been prepared in Bulgarian leva and all amounts have been rounded to the nearest thousand (BGN'000), unless otherwise stated.

Statement of compliance

The financial statements of FLAGB FLAG EAD have been prepared in accordance with the International Financial Reporting Standards, which have been endorsed by the European Union (IFRS, endorsed by EU).

2.2 Summary of significant accounting policies

a) Foreign currency translation

The financial statements are presented in Bulgarian levs, which is also the functional and presentation currency of the Company. Transactions in foreign currencies are initially recorded in the functional currency rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated on a monthly basis by applying the exchange rate published by the Bulgarian National Bank for the last working day of the respective month. All exchange differences are taken to the statement of comprehensive income. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as of the date of initial transaction (acquisition).

b) Revenue recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Company and the revenue can be reliably measured, regardless of the timing of the payment. Revenue is measured at the fair value of the consideration received or due, based on the contractual terms of payment, excluding discounts, rebates, and other sales taxes or duty. The Company analyses its selling agreements according to specific criteria to determine whether it acts as principal or as an agent. It has concluded that it acts as principal in all such arrangements. The following specific recognition criteria must also be met before revenue is recognised:

2.2 Summary of significant accounting policies (continued)

b) Revenue recognition (continued)

Interest income
Interest income is recognised using the effective interest rate, i.e. the interest rate that discounts exactly the estimated future cash flows over the estimated useful life of the financial instrument, or a shorter period where appropriate, to the carrying amount of the financial asset. Interest income is included in the financial income in the statement of comprehensive income.

Rendering of services
Revenue from services rendered is recognised in the period during which the service is performed.

c) Taxes

Current income tax
Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the reporting date. The management analyses the various items in the tax return, when the applicable tax provisions are subject to interpretation and recognises provisions where appropriate.

Current taxes are recognised directly in equity (not in the statement of comprehensive income) if the tax relates to items which have been recognised directly in equity.

Deferred income tax
Deferred income tax is provided using the liability method on all temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts.

A deferred tax liability is recognised for all taxable temporary differences:

- except, where the deferred income tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.
- for temporary taxable differences related to investments in subsidiaries, associates and joint venture interests, except where the Company is able to control the timing of the reversal of the temporary difference and it is probable that the temporary difference would not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses:

- except, where the deferred income tax asset arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- for deductible temporary differences related to investments in subsidiaries, associates and joint venture interests, deferred tax assets is recognised only to the extent it is probable that the temporary difference will reverse within the foreseeable future and taxable profit will be available to utilise the temporary difference.

The carrying amount of deferred income tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised. Unrecognised deferred tax assets are reassessed at each reporting date and are recognised to the extent it has become probable that future taxable profit will be gained, which would allow recovery of the deferred tax asset.

2.2 Summary of significant accounting policies (continued)

c) Taxes (continued)

Deferred income tax (continued)

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

Deferred taxes related to items recognised outside the profit or loss are recognised outside the profit or loss. Deferred taxes are recognised depending on the related transaction either in the other comprehensive income or directly in equity.

Deferred income tax assets and deferred income tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred income taxes relate to the same taxable entity and the same taxation authority.

d) Financial instruments - initial recognition and subsequent measurement

- **Financial assets**

Initial recognition

Financial assets within the scope of IAS 39 *Financial Instruments*: *Recognition and Measurement* are classified as either financial assets at fair value through profit or loss, or loans and receivables, or held to maturity investments, or available for sale financial assets, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. The Company designates the classification of its financial liabilities upon initial recognition.

When financial assets are recognised initially, they are measured at fair value, plus, in the case of financial assets not at fair value through profit or loss, costs directly attributable to the acquisition of the financial asset.

Purchases or sales of financial assets that require the transfer of the asset over a period of time established normally by regulation or practice in the respective market (regular way purchases) are recognised on the date of the transaction, i.e. the date when the Company has committed to buy or sell the asset.

The financial assets of the Company include cash and cash equivalents, loans granted and trade and other receivables.

Subsequent measurement

The subsequent measurement of the financial assets depends on their classification as follows:

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement loans and receivables are subsequently carried at amortised cost using the effective interest method (EIRM) less any allowance for impairment. Amortised cost is calculated taking into account any discounts or premiums on acquisition and fees or expenses inherent to the EIR. EIR amortisation is included in the financial income in the income statement. Impairment losses are taken to the income statement as finance costs.

2.2 Summary of significant accounting policies (continued)

d) Financial instruments - initial recognition and subsequent measurement (continued)

- **Financial assets (continued)**

Derecognition
A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- the rights to receive cash flows from the asset have expired;
- the contractual rights to receive the cash flows from the financial asset are transferred or the Company has the obligation to pay fully the cash flows received without significant delay to a third party under a transfer agreement; where (a) the Company has transferred significantly all risks and rewards from the title over the financial asset; or (b) the Company has neither transferred nor retained significantly all risks and rewards from the title over the financial asset, but has not retained control over the asset.

Where the Company has transferred its rights to receive cash flows from a financial asset and has a transfer agreement and has neither transferred nor retained substantially all the risks and rewards of the financial asset but has retained the control of the asset, the asset is recognised to the extent of the Company's continuing involvement in the asset. In this case the Company recognises the related liability. The transferred asset and the related liability are recognised on basis reflecting the rights and obligations retained by the Company.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Company could be required to repay.

Impairment of financial assets

Financial assets carried at amortised cost

For financial assets carried at amortised cost the Company first assesses individually whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If it is assessed that no objective evidence for impairment exist for individually measured financial asset, regardless of whether it is significant or not, the Company includes the asset in a group of financial assets with similar features of credit risk and reviews them for impairment collectively. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

If objective evidence exist for impairment loss the amount is the difference between the asset's carrying amount and the present value of the expected future cash flows (excluding any future loan losses that have not yet been incurred). The present value of the expected future cash flows is discounted using the original effective interest rate of the financial asset. If a loan has a floating interest rate the discount rate for impairment loss represents the current effective interest rate.

Evidence of impairment may include indications that the debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy/announce over-indebtedness or undertake other financial reorganisation or where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

2.2 Summary of significant accounting policies (continued)

d) Financial instruments - initial recognition and subsequent measurement (continued)

- **Financial assets (continued)**

Financial assets carried at amortised cost

Due to the specific nature of its operations the Company sets aside impairment provisions as follows:

Specific impairment

The purpose of the specific impairment is to adjust the value of specific loans granted for which objective evidence of impairment exists to their recoverable amount and to set aside provisions reflecting the risk of non-repayment of the respective loans.

Impairment on portfolio basis

Impairment is charged in consideration of the common risk nature of the portfolio and takes into account the overall structure of the loan portfolio, the amount of receivables overdue as at the reporting date and the management's expectations as to the recoverable amount of loans granted.

The carrying amount of the asset is written down using an allowance account and the impairment loss is recognised in the statement of comprehensive income. Interest income continues to be accrued on the reduced carrying amount based on the original interest rate of the asset, which is used to discount the future cash flows for the purpose of measurement of the impairment loss.

Loans granted, and the related allowances are written off when no realistic opportunity exists to collect them in the future and all collateral has been realised or has been transferred to the Company. If in a subsequent year the expected impairment loss increases or decreases due to an event occurring after the recognition of the impairment, the impairment loss recognised before is increased or decreased through an adjustment in the allowance account. If the future write-down is recovered at a later stage, the recovery is recognised in the current period result.

- **Financial liabilities**

Initial recognition and measurement

Financial liabilities within the scope of IAS 39 are classified as financial liabilities at fair value through profit or loss or as loans and borrowings, or as derivatives, which are effective hedging instruments, as appropriate. The company designates the classification of its financial liabilities upon initial recognition.

Financial liabilities are initially recognised at fair value, plus in the case of loans and borrowings, the transaction costs directly related to the acquisition of the financial liability.

The Company's financial liabilities include interest-bearing loans and trade and other payables.

2.2 Summary of significant accounting policies (continued)

d) Financial instruments - initial recognition and subsequent measurement (continued)

- **Financial liabilities (continued)**

Subsequent measurement

The subsequent measurement of the financial liabilities depends on their classification as follows:

Loans and borrowings

After initial recognition, loans and borrowings are subsequently measured at amortised cost using the effective interest rate method. Gains and losses on loans and borrowings are recognised in the current period result when the liabilities are derecognised as well as through the amortisation process.

Amortised cost is calculated taking into account any discounts or premiums on acquisition and fees or expenses inherent to the EIR. The amortisation of EIR is included in the interest expense in the statement of comprehensive income.

Derecognition

A financial liability is derecognised when the obligation under the contract is discharged, or cancelled, or expired.

When an existing financial liability is exchange for another liability from the same creditor at significantly different terms or the terms of the existing liability are significantly modified, this exchange or modification is treated as derecognition of the original liability and recognition of a new one, and the difference in the respective carrying amounts is recognised in the profit or loss for the period.

e) Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount is taken to the statement of financial position, if and only if there is a legally enforceable right to offset the recognised amounts and the Company intends to settle the asset and liability on net basis, or to simultaneously realise the assets and settle the liabilities.

f) Fair value of financial instruments

At each reporting date the fair value of financial instruments which are traded actively at the markets is determined based on quoted market prices or quotes from dealers ("buy" prices on long positions and "sell" prices on short positions) without deducting any transaction costs.

The fair values of financial instruments without an active market are determined using appropriate valuation techniques. These techniques include use of recent market transactions between arm's length transactions; references to the current fair value of similar instruments that are significantly the same; analysis of the discounted cash flows, and other valuation models.

Analysis of the fair values of financial instruments and details of their measurement is presented in Note 20.

g) Share capital

Share capital is presented at the nominal amount of the shares issued and paid-in. The Company is obliged to set aside Reserves Fund in accordance with the Commercial Act. Sources for the funds may include:

- portion of the profit set by the sole owner of the capital, but no less than 1/10 until the funds in the Reserves Fund reach 1/10 of the capital;
- funds, received in excess of par value of shares at issue thereof;
- other sources in accordance with decision of the General Assembly.

The Reserves Fund may only be used to cover current and prior year losses. When the Reserves Fund reaches the minimum amount set out in the statutes, any excess may be used for share capital increases.

2.2 Summary of significant accounting policies (continued)

h) Plant and equipment

Plant and equipment are carried at cost less the accumulated depreciation and the accumulated impairment losses, if any. Acquisition cost includes costs related to replacement of parts of the plant and equipment, and borrowing costs on long-term construction contracts, if they meet the criteria for recognition of an asset. When costs are incurred for major inspection of plant and / or equipment these are capitalised in the carrying amount of the respective asset as replacement cost, provided they meet the asset recognition criteria. All other repair and maintenance costs are taken to statement of comprehensive income in the period incurred.

Depreciation is calculated on a straight line basis over the estimated useful life of the assets as follows:

Computers	2 years
Property, plant and equipment	5 years
Transport vehicles	4 years
Fixtures and fittings	5 years

An item of plant and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds, if any, and the carrying amount of the asset) is included in the statement of comprehensive income in the year the asset is derecognised.

The asset's residual values, useful lives and methods of depreciation are reviewed, and adjusted prospectively if expectations differ from the previous estimates, at each financial year end.

i) Cash and cash equivalents

Cash and short-term deposits in the statement of financial position include cash at banks, and on hand and short-term deposits of original maturity of twelve months or less, that are available to the Company on demand without incurring significant financial losses.

For the purpose of the cash flow statement, cash and cash equivalents consist of cash and cash equivalents as defined above.

j) Provisions

General
Provisions are recognised when the Company has a present obligation (legal or constructive) as a result of a past event, when it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Where the Company expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain The expense relating to any provision is presented in the statement of comprehensive income net of any recoveries. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as a finance cost.

2.3 Changes in accounting policies and disclosures

New and amended standards and interpretations

The accounting policies adopted are consistent with those of the previous reporting period except the following new and amended IFRS and Interpretations (IFRIC) to the International Financial Reporting Standards effective as at 1 January 2010:

- IFRS 2 Share-based payments: *Group Cash-settled Share-based Payment Transactions* effective 1 January 2010
- IFRS 3 *Business Combinations (Revised)* and IAS 27 *Consolidated and Separate Financial Statements (Amended)* effective 1 July 2009, including consequential amendments to IFRS 2, IFRS 5 IFRS 7, IAS 7, IAS 21, IAS 28, IAS 31 and IAS 39
- IFRS 39 Financial Instruments: *Recognition and Measurement – Eligible Hedged Items* effective 1 July 2009
- IFRIC 17 *Distributions of Non-cash Assets to Owners* effective 1 July 2009
- Improvements to IFRSs (May 2008 and April 2009)

The adoption of the standards or interpretations is described below:

IFRS 2 Share-based payments (revised)
The IASB issued an amendment to IFRS 2 that clarified the scope and the accounting for group cash-settled share-based payment transactions. The Company adopted this amendment as of 1 January 2010. It did not have an impact on the financial position or performance of the Company.

IFRS 3 Business Combinations (Revised) and IAS 27 Consolidated and Separate Financial Statements (Amended)
IFRS 3 (Revised) introduces significant changes in the accounting for business combinations occurring after becoming effective Changes affect the valuation of non-controlling interest, the accounting for transaction costs, the initial recognition and subsequent measurement of a contingent consideration and business combinations achieved in stages. These changes will impact the amount of goodwill recognised, the reported results in the period that an acquisition occurs and future reported results.

IAS 27 (Amended) requires that a change in the ownership interest of a subsidiary (without loss of control) is accounted for as a transaction with owners in their capacity as owners. Therefore, such transactions will no longer give rise to goodwill, nor will it give rise to a gain or loss. Furthermore, the amended standard changes the accounting for losses incurred by the subsidiary, as well as the loss of control of a subsidiary. The changes by IFRS 3 (Revised) and IAS 27 (Amended) affect acquisitions or loss of control of subsidiaries and transactions with non-controlling interests after 1 January 2010.

As the Company did not report any business combinations, or investments in any subsidiaries, the above revisions and amendments did not have an impact on its financial statements.

IFRS 39 Financial Instruments: *Recognition and Measurement – Eligible Hedged Items*
The amendment clarifies that an entity is permitted to designate a portion of the fair value changes or cash flow variability of a financial instrument as a hedged item. This also covers the designation of inflation as a hedged risk or portion in particular situations. The amendment will have no impact on the financial position of the Company and its performance, as it has not entered into any such hedges.

IFRIC 17 – Distributions of Non-cash Assets to Owners
This interpretation provides guidance on accounting for arrangements whereby an entity distributes non-cash assets to shareholders either as a distribution of reserves or as dividends. The interpretation has no effect on either, the financial position or performance of the Company.

2.3 Changes in accounting policies and disclosures (continued)

New and amended standards and interpretations (continued)

Improvements to IFRSs

In May 2008 and April 2009, the IASB issued omnibus of amendments to its standards, primarily with a view to removing inconsistencies and clarifying wording. There are separate transitional provisions for each standard. These amendments, as listed below, did not have any impact on the accounting policies, financial position or performance of the Company.

- IFRS 2 Share-based payments
- IFRS 5 Non-current Assets Held for Sale and Discontinued Operations
- IFRS 8 Operating segments
- IAS 1 Presentation of Financial Statements
- IAS 7 Cash Flow Statement
- IAS 17 Leases
- IAS 34 Interim Financial Reporting
- IAS 36 Impairment of Assets
- IAS 38 *Intangible Assets*
- IFRS 39 Financial Instruments: *Recognition and Measurement*
- IFRIC 9 Reassessment of Embedded Derivates
- IFRIC 16 Hedges of a Net Investment in a Foreign Operation

Reclassifications

For the purpose of better presentation, understanding and appropriateness of the information presented in the Group's financial statements, the management has considered necessary and has revised the presentation for the prior reporting period of the statement of financial position, income statement and cash flow statement, by reclassifying certain items without having influence on the reported financial position, performance and cash flows.

3. Significant accounting judgments, estimates and assumptions

The preparation of the financial statements requires the management to apply accounting judgements, estimates and assumptions, which have effect on the amount of reported assets and liabilities, and the disclosure of the contingent liabilities at the date of the financial statements, as well as on the income and expenses reported for the period. Uncertainties related to these assumptions and estimates may lead to actual results requiring material adjustments in the carrying amounts of the respective assets or liabilities in subsequent reporting periods.

Estimates and assumptions

The key assumptions concerning the future and other key sources of estimation uncertainty at the date of the statement of financial position, that have a significant risk of causing a material adjustments to the carrying amounts of assets and liabilities within the next reporting period are discussed below:

Impairment of financial receivables

The Company is using an adjustment account to report the allowance on the impairment of doubtful and bad receivables from customers. The management assesses the appropriateness of this impairment based on ageing analysis of the receivables, historical experience as to the write-off rates of bad debts, as well analysis of the solvency of the respective municipality, changes in the contractual payment terms, etc. If the financial position and performance of municipalities deteriorate (in excess of the expected) the amount of the receivables to be written off in the next reporting periods may be higher than the one estimated at the date of the statement of financial position. At 31 December 2010, the best estimate of the management for the necessary provision for impairment of receivables is BGN 143 thousand (2009: nil). Further information is presented in note 11.

4. Standards issued but not yet effective

Standards issued but not yet effective by the date of issue of the financial statements of the Company are listed below. The Company will adopt them as of their respective effective dates.

IAS 12 Income Taxes (Amendment)
The amendment provides a practical solution to the problem of determining whether assets measured using the fair value model in IAS 40 Investment Property are recovered through use or through sale. The amendment is effective for annual periods beginning on or after 1 July 2011. The Company does not expect any impact on their financial position or performance. This amendment has not yet been endorsed by the EU.

IAS 24 Related Party Disclosures (Amendment)
The amended standard is effective for annual periods beginning on or after 1 January 2011. It clarified the definition of a related party to simplify the identification of such relationships and to eliminate inconsistencies in its application. The revised standard introduces a partial exemption of disclosure requirements for government-related entities. The Company does not expect any impact on its financial position or performance.

IAS 32 Financial Instruments: Presentation – Classification of Rights Issues (Amendment)
The amendment to IAS 32 is effective for annual periods beginning on or after 1 February 2010 and amended the definition of a financial liability in order to classify rights issues (and certain options or warrants) as equity instruments in cases where such rights are given pro rata to all of the existing owners of the same class of an entity's non-derivative equity instruments, or to acquire a fixed number of the entity's own equity instruments for a fixed amount in any currency. This amendment will have no impact on the Company's financial statements after initial application.

IFRS 7 Financial Instruments: Disclosures (amendments)
The amendments improve the disclosure requirements in relation to transferred financial assets. They are effective for annual periods beginning on or after 1 July 2011. The amendments are deemed to have no impact on the financial statements of the Company. These amendments have not been endorsed by the EU yet.

IFRS 9 Financial Instruments: Classification and Measurement
IFRS 9 as issued reflects the first phase of the IASBs work on the replacement of IAS 39 and applies to classification and measurement of financial assets as defined in IAS 39. The standard is effective for annual periods beginning on or after 1 January 2013. In subsequent phases, the IASB will address classification and measurement of financial liabilities, hedge accounting and derecognition. The completion of this project is expected in early 2011. The Company is in the process of assessing the impact of IFRS 9 on its financial position and performance. This Standard has not been endorsed by the EU yet.

IFRIC 14 Prepayment of a Minimum Funding Requirement (Amendment)
The amendment to IFRIC 14 is effective for annual periods beginning on or after 1 January 2011 with retrospective application. The amendment provides guidance on assessing the recoverable amount of a net pension asset. The amendment permits an entity to treat the prepayment of a minimum funding requirement as an asset. The amendment is deemed to have no impact on the financial statements of the Company.

IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments
IFRIC 19 is effective for annual periods beginning on or after 1 July 2010. The interpretation clarifies that equity instruments issued to a creditor to extinguish a financial liability qualify as consideration paid. The equity instruments issued are measured at their fair value. In case that this cannot be reliably measured, the instruments are measured at the fair value of the liability extinguished. Any gain or loss is recognised immediately in profit or loss. The adoption of this interpretation will have no effect on the financial statements of the Company.

Improvements to IFRSs (issued in May 2010)
The IASB issued *Improvements to IFRSs*, an omnibus of amendments to its IFRS standards. The amendments have not been adopted as they become effective for annual periods on or after either 1 July 2010 or 1 January 2011. The Company expects no impact from the adoption of the amendments on its financial position and performance.

5. Income and expenses

5.1 Interest income

	2010	2009
	BGN'000	*BGN'000*
Interest income on deposits and bank accounts	5,870	3,570
Income on loans granted and receivables	3,065	1,215
Total interest income	**8,935**	**4,785**

5.2 Interest and fee expense

	2010	2009
	BGN'000	*BGN'000*
Interest expenses on loans and borrowings	2,289	656
Expenses on currency transactions	49	77
Expenses on fees and commissions	525	246
Total interest and fee expense	**2,863**	**979**

5.3 Personnel expenses

	2010	2009
	BGN'000	*BGN'000*
Remuneration	289	284
Social security contributions	37	35
Total personnel expenses	**326**	**319**

5.4 Other operating costs

	2010	2009
	BGN'000	*BGN'000*
Legal services – EBRD	75	109
Rent	71	99
Consulting services	-	58
Accounting and audit services	53	26
Materials	21	16
Computer support	5	7
Communications	8	5
Media	1	3
Translations	2	3
Social	2	2
Insurance	2	2
Other	33	31
Total other operating costs	**273**	**361**

6. Income tax

The main components of the income tax expenses for the years ended 31 December 2010 and 2009 are:

	2010	2009
	BGN'000	*BGN'000*
Current income tax expense	533	314
Deferred tax benefit	-	(1)
Income tax expense	**533**	**313**

The income tax rate applicable for 2010 is 10% (2009: 10%).

The reconciliation between the income tax expense and the accounting profit, multiplied by the applicable tax rate for the years ended 31 December 2010 and 31 December 2009 is presented below:

	2010	2009
	BGN'000	*BGN'000*
Accounting profit before tax	5,338	3,135
Income tax expense at the applicable tax rate of 10% for 2010 (2009: 10%)	534	313
Non-deductible expenses		
Other	(1)	-
Income tax expense	**533**	**313**

7. Cash and cash equivalents

	2010	2009
	BGN'000	*BGN'000*
Cash on hand and at banks	46	1,577
Balances of interest receivable on deposits	2,007	766
Short-term deposits	85,036	64,146
Total cash and cash equivalents	**87,089**	**66,489**

Cash at banks accrue floating interest rates based on the daily interest rates on bank deposits. Short-term deposits have a term of one year with a possibility to change the amounts held in the deposits depending on the liquidity needs of the Company. They accrue interest at the contractual interest rates which vary between 5 and 7.5 % per annum (2009: 7.5-10%). Balances on interest receivable on deposits include cash and cash equivalents as the amounts accrued are available to the Company on demand. The fair value of cash and short-term deposits is equal to their carrying amount.

8. Receivables and prepaid expenses

	2010	2009
	BGN'000	*BGN'000*
Other receivables	7	5
Total receivables and prepaid expenses	**7**	**5**

Other receivables relate to guarantees granted and non-financial deferred expenses.

9. Plant and equipment

	Computers	Fixtures and fittings	Plant and equipment	Motor vehicles	Total
	BGN'000	*BGN'000*	*BGN'000*	*BGN'000*	*BGN'000*
Book value:					
On 1 January 2009	16	7	-	36	59
Additions	4	-	-	-	4
Transfers	(1)	-	1	-	-
Disposals	-	-	-	-	-
On 31 December 2009	19	7	1	36	63
Additions	-	-	1	-	1
Transfers	-	-	-	-	-
Disposals	-	-	-	-	-
On 31 December 2010	19	7	2	36	64
Depreciation:					
On 1 January 2009	(2)	-	-	-	(2)
Depreciation charged for the year	(8)	(2)	-	(9)	(19)
Written off	-	-	-	-	-
On 31 December 2009	(10)	(2)	-	(9)	(21)
Depreciation charged for the year	(8)	(1)	-	(9)	(18)
Written off	-	-	-	-	-
On 31 December 2010	(18)	(3)	-	(18)	(39)
Carrying amount:					
On 1 January 2009	**14**	**7**	**-**	**36**	**57**
On 31 December 2009	**9**	**5**	**1**	**27**	**42**
On 31 December 2010	**1**	**4**	**2**	**18**	**25**

10. Deferred tax assets

As at 31 December 2010 and 31 December 2009 deferred taxes are related to the following:

	Statement of financial position		Statement of comprehensive income	
	2010	2009	2010	2009
	BGN'000	*BGN'000*	*BGN'000*	*BGN'000*
Deferred tax assets				
Unused leave of the personnel	1	1	-	(1)
Deferred tax benefit			**-**	**(1)**
Deferred tax assets, net	**1**	**1**		

11. Loans granted

	2010	2009
	BGN'000	*BGN'000*
Loans granted	47,632	48,461
Impairment of receivables on loans granted	(143)	-
Interest receivable	56	47
Total loans granted	**47,545**	**48,508**

Loans granted represent loans extended to municipalities. Most of the loans granted – BGN 44,429 thousand are used as bridge financing under European programmes. The remaining amount of BGN 3,203 thousand is intended for lending of municipalities' own activities**.**

Loans granted are secured mainly with specific pledges over the future receivables of the municipalities under the grant agreements and the future own revenue of the municipalities.

The movements in the impairment loss provisions of loans granted in 2010 and 2009 are as follows:

	Impairment of receivables on loans granted
Position at 1 January 2009	-
Accrued during the year	-
Reversed during the year	-
Net movements in impairment	**-**
Receivables written off against provisions	-
Position at 31 December 2009	**-**
Accrued during the year	(143)
Reversed during the year	-
Net movements in impairment	**(143)**
Receivables written off against the accumulated impairment	-
Position at 31 December 2010	**(143)**

12. Payables on EBRD loan

	Effective interest rate %	Maturity	2010	2009
			BGN'000	*BGN'000*
Long-term				
Payables on EBRD loan	4.08%	August 2023	68,454	52,061
Deferred fees under contracts with EBRD			(296)	(319)
Accrued interest due			975	554
Total payables on EBRD loan			**69,133**	**52,296**

The payables of the Company to the European Bank for Reconstruction and Development (EBRD) result from the utilisation of funds under loan agreement with a limit of EUR 35,000 thousand (BGN 68,454 thousand), which amount has two components:

1. Loan "a" – at the amount of EUR 18,000 thousand (BGN 35,205 thousand)
2. Loan "b" – at the amount of EUR 17,000 thousand (BGN 33,249 thousand)

The term of the loans is 15 years with a 3-year grace period. The contractual interest rate is based on six-month EURIBOR plus a floating margin of 2.25% to 2.75%, defined based on the existence and amount of bad debt in the Company's loan portfolio. Additional fees are envisaged: (a) annual commitment fee; (b) one-off Front - End Fee; (c) annual administration fee.
As at 31 December 2010 the Company has utilised the fill amount of the loan - EUR 35,000 thousand (BGN 68,454 thousand) – of the resource granted and is not in violation of any covenants of the agreement with EBRD on capital and financial adequacy.

Unutilised loans
As at 31 December 2010 the Company has available unutilised credit line at the total amount of BGN 68,454 thousand in respect of which all contractual terms and conditions have been met. The prepaid fee related to the initial costs to set up the credit line is presented in the statement of financial position and is carried in the statement of comprehensive income under the straight-line method over the term of the loan. As at 31 December 2010 the remaining amount of the prepaid expenses for the initial fee is BGN 660 thousand (2009: BGN 722 thousand).

13. Payables to personnel and social security contributions

As at 31 December 2019 payables to the personnel and social security contributions are related to current remuneration for December 2010 as well as additional remuneration (bonuses) accrued. They are allocated as follows

	2010	2009
	BGN'000	*BGN'000*
Payables to the personnel	40	47
Payables on social security contributions	9	10
Total payables to personnel and social security contributions	**49**	**57**

14. Taxes payable

As at 31 December 2010 taxes payable are current and include:

	2010	2009
	BGN'000	*BGN'000*
Income tax	209	253
Total taxes payable	**209**	**253**

The movements in taxes payable in 2010 and 2009 are as follows:

	2010	2009
	BGN'000	*BGN'000*
Taxes payable as at 31 January	**(253)**	**(72)**
Tax paid during the year	577	132
Tax accrued for the year	(533)	(313)
Taxes payable at 31 December	**(209)**	**(253)**

15. Share capital and reserves

15.1 Share capital

	2010	2009
	BGN'000	*BGN'000*
60,000 ordinary shares at a par value of BGN 1,000 each	60,000	60,000
Total share capital	**60,000**	**60,000**

As at 31 December 2010 and 31 December 2009 the issued registered capital is fully paid-in.

15.2 Statutory reserves

Statutory reserves are formed by FLAGB FLAG EAD as a distribution of the profit as provided for under art. 246 of the Commercial Act. They are set aside until the amount reaches one tenth or more of the capital. Sources to form the statutory reserves include at least one tenth of the net profit, share premiums and funds set out in the statutes or in accordance with a decision of the general assembly of the shareholders.
The statutory reserves may only be used to cover current and prior reporting period losses. As at 31 December 2010 statutory reserves amount to BGN 342 thousand (2009: BGN 60 thousand).

16. Related party disclosures

Composition of related parties

Shareholder – sole owner

The Republic of Bulgaria through the Ministry of Regional Development and Public Works is the sole owner of the shares of FLAGB FLAG EAD.

Other related parties

All state-owned companies and companies with state interest are related parties to the Company.

Related party transactions

In 2007, 2008, 2009 and 2010 there have been no closed and / or implemented related party transactions.

17. Dividend distribution

In accordance with art. 25 of Decree 324 of the Council of Ministers dated 30 December 2009 in 2010 dividends are distributed to the sole shareholder at the amount of BGN 2,031 thousand (2009: BGN 271 thousand). Dividends per share amount to BGN 33.85 (2009: BGN 4.52).

18. Commitments and contingencies

Lawsuits

As at 31 December 2010 and 31 December 2009 there are no lawsuits filed against the Company.

Guarantees

As at 31 December 2010 and 31 December 2009 the Company has not extended any guarantees.

Other

On 3 July 2009 a second loan agreement was signed between the Fund and the European Bank for Reconstruction and Development (EBRD). The amount of the loan agreed which EBRD will extend to the Company has a ceiling of EUR 35,000 thousand (BGN 68,454 thousand). This amount will be utilised in two tranches:

Loan “a” at an amount not exceeding EUR 30,000 thousand (BGN 58,675 thousand)

Loan "b" at an amount not exceeding EUR 5,000 thousand (BGN 9,792 thousand)

The purpose of the loan is for the Company to provide loans to municipalities having certain creditworthiness, which is insufficient for independent use of borrowings at the market in Bulgaria.

The term of the loan is 12 years with a 2-year grace period. The agreed interest rate is based on six-month EURIBOR plus a floating margin of 3.25% to 3.75%, depending on the existence of bad debt in the Company's loan portfolio. Additional fees are envisaged as follows: (a) annual commitment fee; (b) one-off Front - End Fee; (c) annual administration fee.

19. Financial risk management objectives and policy

The main financial liabilities of the Company include interest bearing loans and borrowings, and trade payables. The main objective of these financial instruments is to secure financing for the Company's operations. The Company holds financial assets, such as loans granted, cash and short-term deposits which arise directly from its operations.

In 2010 and 2009 the Company did not hold and trade with derivative financial instruments.

The main risks arising from the Company's financial instruments include interest rate risk, liquidity risk, foreign currency risk, and credit risk. The policy adopted by the Company's management to manage these risks is summarised below.

Interest rate risk

The Company is exposed to the risk of changes in the market interest rates, mainly in respect of its floating rate long-term financial liabilities. The Company's policy is to manage interest expense through the extension of floating interest rate loans.

The table below presents a sensitivity analysis to the possible changes in the interest rates and their effect on the profit before tax (through the effect on floating interest rate liabilities and floating interest rate loans granted), if all other variables remain constant.

	Increase/ decrease in interest rates	Effect on profit before tax
		BGN'000
2010		
In EUR	+0.5%	(342)
In BGN	+0.5%	238
In EUR	-1%	684
In BGN	-1%	(476)
2009		
In EUR	+0.5%	(260)
In BGN	+0.5%	242
In EUR	-1%	521
In BGN	-1%	(485)

Liquidity risk

The effective management of the Company's liquidity requires ensuring sufficient working capital, mainly through maintaining unutilised approved credit facilities**.**

19. Financial risk management objectives and policy (continued)

Liquidity risk (continued)

As at 31 December the maturity structure of the Company's financial assets and financial and other liabilities, based on agreed undiscounted payments, is presented in the tables below:

Liabilities
As at 31 December 2010

	Demand	< 3 months	3-12 months	1-5 years	> 5 years	Total
	BGN'000	*BGN'000*	*BGN'000*	*BGN'000*	*BGN'000*	*BGN'000*
Interest bearing loans and borrowings	-	1,360	1,360	39,571	45,881	88,172
Trade and other payables	-	267	-	-	-	267
	-	267	975	22,818	45,636	69,696

As at 31 December 2009

	Demand	< 3 months	3-12 months	1-5 years	> 5 years	Total
	BGN'000	*BGN'000*	*BGN'000*	*BGN'000*	*BGN'000*	*BGN'000*
Interest bearing loans and borrowings	-	1,034	1,034	26,489	40,468	69,125
Trade and other payables	-	318	-	-	-	318
	-	318	554	17,114	34,947	52,933

The maturity structure of assets and liabilities as at 31 December 2010 is drawn up based on the expectations of the management regarding the recovery / settlement of amounts:

Assets	*Up to 1 year*	*Over 1 year*	***Total***
Cash and cash equivalents	87,089	-	**87,089**
Receivables and prepaid expenses	7	-	**7**
Loans granted	39,571	7,974	**47,545**
Deferred tax assets	-	1	**1**
Plant and equipment	-	25	**25**
Prepaid initial costs on fees on EBRD loan	55	605	**660**
Total assets	**126,722**	**8,605**	**135,327**

19. Financial risk management objectives and policy (continued)

Liquidity risk (continued)

Liabilities	*Up to 1 year*	*Over 1 year*	***Total***
Payables to personnel and social security contributions	49	-	**49**
Taxes payable	209	-	**209**
Other payables	9	-	**9**
Payables on EBRD loan	927	68,206	**69,133**
Total liabilities	**1,194**	**68,206**	**69,400**

The maturity structure of assets and liabilities as at 31 December 2009 is drawn up based on the expectations of the management regarding the recovery / settlement of amounts:

Assets	*Up to 1 year*	*Over 1 year*	***Total***
Cash and cash equivalents	66,489	-	**66,489**
Receivables and prepaid expenses	5	-	**5**
Loans granted	41,129	7,379	**48,508**
Deferred tax assets	-	1	**1**
Plant and equipment	17	25	**42**
Prepaid initial costs on fees on EBRD loan	62	660	**722**
Total assets	**107,702**	**8,065**	**115,767**

Liabilities	*Up to 1 year*	*Over 1 year*	***Total***
Payables to personnel and social security contributions	57	-	**57**
Taxes payable	253	-	**253**
Other payables	8	-	**8**
Payables on EBRD loan	531	51,765	**52,296**
Total liabilities	**849**	**51,765**	**52,614**

Foreign currency risk

The Company has no purchases, sales and does not grant loans in foreign currencies and the loans received are denominated in EUR. Since the exchange rate BGN / EUR is fixed to 1.95583, the currency risk resulting from the Company's exposures in EUR is not significant.

Credit risk

Credit risk is the risk that the clients / counterparties will be unable to pay in full amounts due to the Company within the envisaged / agreed deadlines. At the end of 2010 the remaining liability of municipalities to the Company amounts to BGN 47,632 thousand.

Credit risk management in 2010 is carried out by the "Lending" Directorate and is monitored simultaneously by the Executive Director and the Board of Directors. The credit risk management function is to ensure the implementation of appropriate investment policy in respect of the funds available and accordingly – the compliance of this policy with the related procedures and controls for current monitoring of the respective loan, deposit or receivable.

19. Financial risk management objectives and policy (continued)

Credit risk (continued)

Risk credit exposure is managed through current analysis of the ability of the counterparties / servicing banks to comply with their contractual obligations to pay interest and principal, and through setting appropriate credit limitations. Cash deposits are placed with prime banks having good reputation at the Bulgarian market. Furthermore, monitoring is carried out currently for existence of concentration of receivables with certain counterparty, and if such is found – the respective counterparty is subject to special current supervision. The impairment accrued on loans granted as at 31 December 2010 is portfolio based, and not in respect of specific exposures.

The maximum exposure of the Company to credit risk as at 31 December 2010 and 31 December 2009 is as follows:

	2010		*2009*	
	Gross maximum exposure	*Net*	*Gross maximum exposure*	*Net*
Exposure				
Cash and cash equivalents	87,088	87,088	66,489	66,489
Loans granted	47,688	47,545	48,508	48,508
Receivables and prepaid expenses	7	7	5	5
Total balance sheet items	**47,695**	**47,552**	**48,513**	**48,513**

The Company allocates its financial assets in several classification groups to assess their credit risk. The table below shows the classification of the gross financial assets in the statement of financial position depending on their default as at 31 December 2010:

	Neither overdue, nor impaired	*Overdue, but not impaired*	*Impaired*	***Total***
Cash and cash equivalents	87,089	-	-	**87,089**
Loans granted	46,386	1,302	-	**47,688**
Receivables and prepaid expenses	7	-	-	**7**
	133,482	**1,302**	**-**	**134,784**

Receivables overdue, but not impaired have been overdue for up to 40 days.

19. Financial risk management objectives and policy (continued)

Credit risk (continued)

The classification of the gross financial assets in the balance sheet depending on their default as at 31 December 2009 is as follows:

	Neither overdue, nor impaired	*Overdue, but not impaired*	*Impaired*	***Total***
Cash and cash equivalents	66,489	-	-	**66,489**
Loans granted	48,298	210	-	**48,508**
Receivables and prepaid expenses	5	-	-	**5**
	114,792	**210**	**-**	**115,002**

Receivables overdue, but not impaired have been overdue for up to 40 days.

Capital management

The primary objective of the Company's capital management is to ensure that it maintains a strong credit rating and healthy capital rations in order to support its business and maximise shareholder value.

The Company manages its capital structure and makes adjustments to it, in light of changes in economic conditions. The Company is subject of Decrees of the Council of Ministers for dividend distribution to the Ministry of Regional Development and Public Works. In 2010 and 2009 there have been no changes in the objectives, policies or processes regarding the Company's capital management.

The Company monitors its equity through the reporting period's financial result as follows:

	2010	**2009**
	BGN'000	*BGN'000*
Net profit in BGN thousand	**4,805**	**2,822**

The Company should comply with externally imposed capital requirements in accordance with bank loan received. They require compliance with certain financial ratios, amongst which is the debt to equity ratio, which should not exceed 7:3. The Company has met the externally imposed capital requirements as at 31 December 2010 and 31 December 2009.

	2010	2009
	BGN'000	*BGN'000*
Interest bearing loans and borrowings	68,454	52,061
Share capital	60,000	60,000
Statutory reserves	342	60
Retained earnings	5,585	3,093
Equity	**65,927**	**63,153**

20. Financial instruments

Fair values

The fair value is the amount at which a financial instrument may be exchanged or settled in an arm's length transaction between willing and knowledgeable parties as best proof of its market value in an active market.

The estimated fair value of the financial instruments is determined by the Company on the basis of available market information, if any, or proper valuation models otherwise. The fair value of financial instruments which are traded actively at organised financial markets is determined based on the "ask" quotes at the end of the last working day of the reporting period. The fair value of financial instruments for which no active market exists is determined using valuation models. These models include the use of recent market transactions between knowledgeable, willing and honest parties; use of the current fair value of another instrument having similar features; analysis of the discounted cash flows or other valuation techniques.

The management of FLAGB FLAG EAD believes that the fair values of the financial instruments which include cash and short-term deposits, trade and other receivables, interest bearing loans and borrowings, trade and other payables do not differ from their carrying amounts as they are of a short-term nature and the applicable interest rates move in unison with the market conditions. The Company has analysed the fair values of fixed interest rate deposits and believes that they approximate their carrying amounts.

21. Events after the reporting date

Except as disclosed above no events have occurred after 31 December 2010 that may require additional adjustments and / or disclosures in the Company's financial statements for the year ended 31 December 2010.