Consolidated Interim Financial Statements
30 September 2012

MP Bank hf. • Ármúli 13a • 108 Reykjavík • Iceland • Reg. no. 540502-2930

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Endorsement and Statement
by the Board of Directors and the CEO

The Consolidated Interim Financial Statements of MP Bank hf. for the period 1 January to 30 September 2012 have been prepared in accordance with International Financial Reporting Standards (IFRSs) for Interim Financial Statements (IAS 34) as adopted by the European Union, and additional Icelandic disclosure requriements. The Consolidated Interim Financial Statements comprise MP Bank hf. and its subsidiaries. The Financial Statements for the year 2011 were approved on 28 February 2012.

According to the Consolidated Income Statement, profit for the period 1 January to 30 September 2012 amounted to ISK 372 million. According to the Consolidated Statement of Financial Position, the Bank's equity at the end of this period amounted to ISK 5,399 million. As at 30 September 2012, the Bank's total assets amounted to ISK 73,172 million. The Tier 1 capital ratio of the Bank was 14.3% but the minimum requirement by law is 8.0%.

The Bank's share capital amounted to ISK 5,554 million as at 30 September 2012 (2011: ISK 5,554 million). The Bank held treasury shares with a nominal value of ISK 4 million (2011: ISK 4 million).

The Bank had 50 shareholders at the end of the period (2011: 51). One shareholder held more than 10% of shares in the Bank, Títan B ehf. with 17.3%.

The Bank had no operations at the start of 2011. On 1 April 2011 the Bank signed a contract acquiring the Icelandic and Lithuanian assets and operations of EA Fjárfestingarfélag hf. (formerly MP Bank hf.) and resumed commercial banking activities on 12 April 2011. Comparative information in the Income Statement and Statement of Cash Flows, and accompanying notes, is therefore not fully comparable.

Corporate Governance

The Board of Directors emphasizes good corporate governance and following accepted guidelines on corporate governance. The Board has laid down comprehensive rules, *The Rules of Procedures for the Board of MP Bank*, in which the authority of the Board is defined and its scope of work in conjunction with the CEO. They cover e.g. order at meetings, competence of Board members to participate in individual decisions, confidentiality and information disclosure between the CEO and the Board. Majority of Board members are independent of the Bank and there are no executive directors on the Board.

The Board determines compensation for the CEO. The Board of Directors has delegated certain tasks to two subcommittees, the Remuneration Committee and the Audit Committee. Each committee has three members appointed by the Board.

Statement by the Board of Directors and the CEO

To the best of our knowledge the Consolidated Interim Financial Statements of MP Bank hf. for the period 1 January to 30 September 2012 comply with IAS 34 "Interim Financial Statements" as adopted by the EU, and give a true and fair view of the Bank's assets, liabilities and financial position as at 30 September 2012 and the financial performance of the Bank and changes of cash flows for the period 1 January to 30 September 2012.

Further, in our opinion the Consolidated Interim Financial Statements and the Endorsement of the Board of Directors and the CEO gives a fair view of the development and performance of the Bank's operations and its position and describes the principal risks and uncertainties faced by the Bank.

The Board of Directors and the CEO of the Bank have today discussed the Consolidated Interim Financial Statements for the period 1 January to 30 September 2012 and confirm them by the means of their signatures.

Reykjavík, 22 November 2012.

Board of Directors

Þorsteinn Pálsson.

Hanna Katrín Friðriksson

Ingvi B. Hrafnsson.

CEO

Independent Auditor's Report

To the Board of Directors and Shareholders of MP Bank hf.

We have reviewed the accompanying consolidated statement of financial position of MP Bank hf. as at 30 September 2012 and the related consolidated statements of comprehensive income, changes in equity and cash flows for the nine-month period then ended and a summary of significant accounting policies and other explanatory information. Management is responsible for the preparation and presentation of this consolidated interim financial information in accordance with IAS 34 "Interim Financial Reporting". Our responsibility is to express a conclusion on this consolidated interim financial information based on our review.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements 2410 *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying consolidated interim financial information is not prepared, in all material respects, in accordance with IAS 34 "Interim Financial Reporting".

Reykjavík, 22 November 2012.

KPMG ehf.

Ól. S. Helgason

Hrafnhildur Helgadóttir

MP Bank hf. Amounts are in ISK thousands

Consolidated Income Statement

For the period 1 January 2012 to 30 September 2012

	Notes	Q3 2012	Q3 2011*	9m 2012	9m 2011*
Interest income		856,482	461,020	2,517,582	816,270
Interest expense		(404,119)	(280,093)	(1,214,171)	(680,497)
Net interest income	58	452,363	180,928	1,303,412	135,774
Fee and commission income	59	381,678	155,360	1,069,605	248,714
Fee and commission expense		(22,058)	(14,360)	(86,882)	(35,508)
Net fee and commission income		359,619	141,000	982,723	213,205
Net financial income	60-61	154,237	46,037	477,832	237,826
Share in profit or loss of associates	74	0	3,679	217,482	(12,675)
Other operating income		14,252	6,754	7,006	19,632
Other operating income		168,489	56,471	702,320	244,784
Net operating income		980,472	378,399	2,988,455	593,763
Administrative expenses	62	(684,369)	(523,496)	(2,238,603)	(1,261,262)
Impairment of loans and receivables	72	(26,376)	(20,983)	(280,145)	(179,500)
Profit (loss) before taxes		269,728	(166,080)	469,707	(846,999)
Income tax	64	6,623	38,530	(32,018)	177,515
Special tax on financial institutions	65	(22,473)	(18,905)	(65,308)	(37,205)
Profit (loss) for the period		253,878	(146,454)	372,380	(706,689)

	Notes	Q3 2012	Q3 2011*	9m 2012	9m 2011*
Attributable to the shareholders of MP Bank hf.		254,741	(144,001)	373,243	(706,689)
Attributable to non-controlling interest		(863)	(2,454)	(863)	0
Profit (loss) for the period		253,878	(146,454)	372,380	(706,689)

The notes on pages 8 to 42 are an integral part of these Consolidated Interim Financial Statements.
**Comparative information is unreviewed, see note 2.*

MP Bank hf. Amounts are in ISK thousands

Consolidated Statement of Comprehensive Income

For the period 1 January 2012 to 30 September 2012

	Notes	9m 2012	9m 2011*
Profit (loss) for the period		372,380	(706,689)
Fair value changes in securities classified as available for sale		(87,248)	52,851
Exchange difference on translation of foreign operations		(3,413)	(451)
Other comprehensive income, net of tax		(90,661)	52,400
Total comprehensive income (loss) for the period		281,719	(654,289)

	Notes	9m 2012	9m 2011*
Attributable to the shareholders of MP Bank hf.		282,582	(654,289)
Attributable to non-controlling interest		(863)	0
Total comprehensive income (loss) for the period		281,719	(654,289)

The notes on pages 8 to 42 are an integral part of these Consolidated Interim Financial Statements.
**Comparative information is unreviewed, see note 2.*

MP Bank hf. Amounts are in ISK thousands

Consolidated Statement of Financial Position

As at 30 September 2012

Assets	Notes	30.9.2012	31.12.2011
Cash and cash equivalents	67	29,583,967	11,545,143
Receivables from Central Bank		8,309,760	0
Fixed income securities	68	5,606,042	13,678,864
Shares and other variable income securities	69	1,080,460	1,068,531
Securities used for hedging	70	1,728,625	7,694,837
Loans to customers	71-72	23,611,085	13,294,303
Derivatives		233,806	199,571
Investment in associates	74	557,913	405,272
Intangible assets	75	1,114,707	1,123,857
Property and equipment	76	754,706	328,599
Deferred tax asset		79,237	107,872
Other assets	77	511,698	662,246
Total assets		73,172,007	50,109,096
Equity			
Share capital	83	5,550,000	5,550,000
Share premium		7,500	7,500
Other reserves		35,928	(8,478)
Accumulated deficit		(194,081)	(480,076)
Total equity attributable to the shareholders of MP Bank hf.		5,399,347	5,068,945
Equity attributable to non-controlling interest		(713)	9
Total equity		5,398,634	5,068,954
Liabilities			
Deposits	78	44,369,409	34,594,083
Borrowings	79	9,165,158	2,051,155
Short positions in securities	80	4,864,286	4,838,963
Short positions in securities used for hedging	81	4,020,156	1,274,229
Derivatives		121,245	101,498
Current tax liabilities		68,697	32,704
Deferred tax liabilities		303	303
Other liabilities	82	5,164,119	2,147,207
Total liabilities		67,773,373	45,040,142
Total equity and liabilities		73,172,007	50,109,096

The notes on pages 8 to 42 are an integral part of these Consolidated Interim Financial Statements.

MP Bank hf. Amounts are in ISK thousands

Consolidated Statement of Changes in Equity

For the period 1 January 2012 to 30 September 2012

1 January 2012 to 30 September 2012	Notes	Share capital	Share premium	Other reserves	Accumulated deficit	Total shareholders' equity	Non-controlling interest	Total equity
Equity at 1 January 2012		5,550,000	7,500	(8,478)	(480,076)	5,068,945	9	5,068,954
Total comprehensive income for the period				(3,413)	285,995	282,582	(863)	281,719
Non-controlling interest acquired	73					0	141	141
Equity instrument related to the acquisition of ALFA verðbréf hf.	73			47,819		47,819		47,819
Equity at 30 September 2012		5,550,000	7,500	35,928	(194,081)	5,399,347	(713)	5,398,634

1 January 2011 to 30 September 2011	Notes	Share capital	Share premium	Other reserves	Accumulated deficit	Total shareholders' equity	Non-controlling interest	Total equity
Equity at 1 January 2011		100,000	330,000		(410,847)	19,153		19,153
Total comprehensive income for the period					(654,289)	(654,289)		(654,289)
New share capital sold		5,400,000				5,400,000		5,400,000
Expenses incurred in relation to share capital increase					(68,750)	(68,750)		(68,750)
Share premium offset against accumulated deficit			(330,000)		330,000	0		0
Equity at 30 September 2011		5,500,000	0	0	(803,885)	4,696,115	0	4,696,115

The notes on pages 8 to 42 are an integral part of these Consolidated Interim Financial Statements.
**Comparative information is unreviewed, see note 2.*

MP Bank hf. Amounts are in ISK thousands

Consolidated Statement of Cash Flows

For the period 1 January 2012 to 30 September 2012

Cash flows from operating activities	Notes	9m 2012	9m 2011*
Profit (loss) for the period		372,380	(706,689)
Adjustments for:			
Indexation and exchange rate difference		59,011	296,305
Effects of associates	74	(217,482)	16,354
Depreciation and amortization	75-76	86,289	51,979
Impairment of loans and receivables	72	280,145	184,250
Deferred income tax, change		28,635	(177,515)
Other adjustments		22,913	0
		631,891	(335,316)
Loans, change		(10,533,909)	(1,099,578)
Deposits, change		9,626,923	3,670,630
Financial assets, change		5,595,862	(1,389,079)
Financial liabilities, change		2,838,816	762,361
Change in operating assets and liabilities		3,203,453	(5,135,566)
Net cash from (to) operating activities		11,363,036	(3,526,548)

Cash flows from investing activities			
Associated companies	74	42,607	27,620
Investment in intangible assets	75	(29,782)	15,513
Investment in property, plant and equipment	76	(493,059)	(17,955)
Disposals of property, plant and equipment	76	20,308	0
Net cash (to) from investing activities		(459,926)	25,178

Cash flows from financing activities		
Borrowings	28,055,002	170,000
Repayment of borrowings	(20,941,000)	(110,000)
New share capital	0	5,331,250
Net cash from financing activities	7,114,002	5,391,250

Cash and cash equivalents at the beginning of the year	11,545,143	0
Net increase in cash and cash equivalents	18,017,112	1,889,880
Cash acquired through business combinations	0	13,945,540
Effects of exchange rate fluctuations on cash held	21,711	17,200
Cash and cash equivalents at the end of the period	29,583,967	15,852,620

The notes on pages 8 to 42 are an integral part of these Consolidated Interim Financial Statements.
**Comparative information is unreviewed, see note 2.*

Notes

General information

1. Reporting entity

MP Bank hf. is a limited liability company incorporated and domiciled in Iceland, with registered offices at Ármúli 13a, Reykjavík. The Consolidated Interim Financial Statements for the period ended 30 September 2012 comprise MP Bank hf. (the Parent) and its subsidiaries (together referred to as the Bank).

The Consolidated Interim Financial Statements were approved and authorised for issue by the Board of Directors of MP Bank hf. on 22 November

2. Basis of preparation

a. Statement of compliance
The Consolidated Interim Financial Statements are condensed and have been prepared in accordance with International Financial Reporting Standard IAS 34, Interim Financial Statements, as adopted by the European Union.

The Consolidated Interim Financial Statements do not include all of the information required for full Consolidated Financial Statements, and should be read in conjunction with the Bank's Consolidated Financial Statements for the financial year ending 31 December 2011, which are available at www.mp.is.

b. Basis of measurement
The Consolidated Interim Financial Statements have been prepared using the historical cost basis except for derivative financial instruments, financial instruments at fair value through profit or loss, available for sale financial assets and securities used for hedging, which are measured at fair value.

c. Functional and presentation currency
The Consolidated Interim Financial Statements are prepared in Icelandic Krona (ISK), which is the Bank's functional currency. All financial information has been rounded to the nearest thousand, unless otherwise stated.

d. Going concern
The Bank's management has assessed the Bank's ability to continue as a going concern and is satisfied that the Bank has the resources to continue its operations.

e. Estimates and judgement
The preparation of interim financial statements in accordance with IFRSs 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.

The estimates and underlying assumptions are based on historical result and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying amounts of assets and liabilities that are not readily apparent from other sources.

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

Information about areas of estimation uncertainty and critical judgements made by management in applying accounting policies that can have a significant effect on the amounts recognised in the Consolidated Interim Financial Statements is provided in note 37.

f. Comparative information
The Bank had no operations at the start of 2011. On 1 April 2011 the Bank signed a contract acquiring the Icelandic and Lithuanian assets and operations of EA Fjárfestingarfélag hf. (formerly MP Bank hf.) and resumed commercial banking activities on 12 April 2011. Comparative information in the Income Statement and Statement of Cash Flows, and accompanying notes, is therefore not fully comparable.

Comparative information in the Consolidated Income Statement, Consolidated Statement of Comprehensive Income, Consolidated Statement of Changes in Equity, Consolidated Statement of Changes in Cash Flows, and accompanying notes, has not been reviewed by the Bank's Auditor.

Notes

Significant accounting policies

3. Basis of consolidation

a. Subsidiaries
Subsidiaries are entities controlled by the Bank. Control exists when the Bank has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Control usually exists when the Bank holds more than 50% of the voting power of the subsidiary. In assessing control, potential voting rights that are presently exercisable or convertible, if any, are taken into account. The financial statements of subsidiaries are included in the financial statements of the Bank from the date that control commences until the date that control ceases.

The Bank uses the purchase method to account for the acquisition of subsidiaries. The cost of an acquisition is measured as the fair value, at the date of exchange, of the assets given, liabilities incurred or assumed and equity instruments issued. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest.

The excess of the cost of acquisition over the fair value of the Bank's share of the identifiable net assets acquired is recognised as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised immediately in the income statement.

b. Non-controlling interest
Non-controlling interest represent the portion of profit or loss and equity not owned, directly or indirectly, by the Bank. Non-controlling interest is presented separately in the income statement and is included in equity in the statement of financial position, separately from equity attributable to owners of the Bank.

The Bank chooses on an acquisition-by-acquisition basis whether to measure non-controlling interest in an acquiree at fair value or according to the proportion of non-controlling interests in the acquiree's net assets. Changes in the Bank's ownership interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions. In such circumstances the carrying amounts of the controlling and non-controlling interests are adjusted to reflect the changes in their relative interests in the subsidiary. Any difference between the amount by which the non-controlling interest is adjusted and the fair value of the consideration paid or received is recognised directly in equity and attributed to the owners of the Bank.

c. Fiduciary services
The Bank provides custody services, fund management and discretionary and advisory investment management services which require the Bank to make decisions on the handling, acquisition or disposal of financial instruments on behalf of its clients.

The financial statements of managed funds, and investment portfolios manage by the Bank on behalf of customers, are not included in the financial statements of the Bank, as they do not constitute Bank assets or liabilities.

d. Transactions eliminated on consolidation
Intra-bank balances, income and expenses, and unrealised gains and losses arising from intra-bank transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with associates are eliminated against the investment to the extent of the Bank's interest in the associate. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

4. Associates

Associates are those entities in which the Bank has significant influence, but not control, over the financial and operating policies. Significant influence generally exists when the Bank holds between 20% and 50% of the voting power, including potential voting rights, if any. Investments in associates are initially recognised at cost.

The Bank's share of the total recognised gains and losses of associates is included in the financial statements of the Bank on an equity accounted basis, from the date the significant influence commences until the date it ceases.

If the Bank's share of loss exceeds its interest in an associate, the Bank's carrying amount is reduced to zero and recognition of further losses is discontinued except to the extent that the Bank has incurred legal or constructive obligations or made payments on behalf of the associate. If the associate subsequently reports profits, the Bank resumes recognising its share of those profits only after its share of the profits equals the share of losses not recognised.

Notes

5. Foreign currency

a. Foreign currency transactions

Transactions in foreign currencies are translated into the respective functional currency of the operation using the exchange rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated to the functional currency using the exchange rate at the reporting date. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated using the exchange rate at the date the fair value was determined.

b. Foreign operations

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated into the functional currency at spot exchange rate current at the reporting date. The income and expenses of foreign operations are translated into the functional currency at the spot exchange rates at the dates of the transactions.

6. Recognition and derecognition of financial assets and liabilities

a. Recognition

Loans, deposits, debt securities issued and subordinated liabilities are recognised on the date that they are originated. All other financial assets and liabilities, including assets and liabilities designated at fair value through profit or loss, are initially recognised on the trade date at which the Bank becomes a party to the contractual provisions of the instrument.

b. Derecognition

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

Financial liabilities are derecognised when the obligation of the Bank is discharged, cancelled or expires.

7. Offsetting

Financial assets and liabilities are offset, and the net amount reported in the statement of fiancial position, 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.

Income and expenses are presented on a net basis for gains and losses arising from a group of similar transactions, such as in the Bank's trading activity, or other circumstances permitted by International Financial Reporting Standards.

8. Amortised cost measurement of financial assets and liabilities

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

9. Financial guarantees

Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

Financial guarantee liabilities are initially recognised at their fair value, and initial fair value is amortised over the life of the financial guarantee. The guarantee liability is subsequently carried at the higher of this amortised amount and the present value of any expected payment, when a payment under the guarantee has become probable. Financial guarantees are included within other liabilities.

Notes

10. Financial instruments - accounting classification

Upon initial recognition, financial assets and liabilities are classified into one of six categories. This classification determines amongst other things initial measurement, subsequent accounting and handling of interest revenue and expenses. International Financial Reporting Standards restrict the reclassification of financial instruments after initial recognition.

a. Held for trading
A financial instrument is classified as held for trading if it is purchased or incurred with the intention to resell, repurchase, repay or collect within a short period of time, or if it is a part of a group of defined financial instruments managed on a portfolio basis and historical data shows recent pattern of short-term profit taking.

Financial assets held for trading include fixed income securities, shares and other variable income securities and derivatives. Financial liabilities include derivatives and short positions, i.e. commitments to deliver financial assets that the Bank has borrowed and sold to a third party.

Financial instruments held for trading are initially recognised at fair value. They are subsequently measured at fair value in the statement of financial position, with transactions costs recognised in profit or loss. Interest income and expense, and all changes in fair value, are recognised as financial income.

b. Designated at fair value
A financial instrument is designated at fair value through profit and loss when it is a part of a portfolio of financial instruments that are managed on the basis of fair value and information provided to management is based on fair value.

Financial assets designated at fair value include fixed income securities and shares and other variable income securities. Financial liabilities consist primarily of short positions, i.e. commitments to deliver financial assets that the Bank has borrowed and sold to a third party.

Financial instruments designated at fair value are initially recognised at fair value. They are subsequently measured at fair value in the statement of financial position, with transactions costs recognised in profit or loss. Interest income and expense, and all changes in fair value, are recognised as financial income.

c. Available for sale
Non-derivative assets with fixed or determinable payments and fixed maturity that the Bank has the positive intent and ability to hold indefinitely, but not necessarily to maturity, are classified as available for sale.

Financial assets classified as available for sale consist primarily of fixed income securities.

Financial instruments classified as available for sale are initially recognised at fair value. They are subsequently measured at fair value in the statement of financial position, with interest income recognised using the effective interest method. The difference between fair value and amortised cost is recognised in comprehensive income until the financial instrument is sold or reaches maturity, whereupon the cumulative gains or losses previously recognised in other comprehensive income are reclassified to financial income.

d. Held to maturity
Non-derivative assets with fixed or determinable payments and fixed maturity that the Bank has the positive intent and ability to hold to marturity are classified as held to maturity.

Financial assets classified as held to maturity consist primarily of fixed income securities.

Financial assets classified as held to maturity are initially recognised at cost. They are subsequently measured at amortised cost using the effective interest method, with interest income recognised in net interest income.

A sale or reclassification of a more than insignificant amount of held to maturity investments would result in the reclassification of all held to maturity investments as available for sale, and would prevent the Bank from classifying investment securities as held to maturity for the current and the following two financial years.

e. Loans and receivables
Non-derivative financial assets with fixed or determinable payments that are not quoted in an active market are classified as loans and receivables.

Financial assets classified as loans and receivables include cash and cash equivalents, loans to customers and receivables.

Financial assets classified as loans and receivables are initially recognised at fair value, which is typically equal to cost, i.e. cash advanced plus any transaction costs. They are subsequently measured at amortised cost using the effective interest method. Accrued interest, in the case of interest bearing assets, is included in the carrying amount. Interest income is recognised in net interest income.

f. Other at amortised cost
Non-derivative financial liabilities with fixed or determinable payments that are not quoted in an active market are classified as other at amortised cost.

Financial liabilities classified as other at amortised cost include deposits, borrowings and payables.

Financial liabilities classified as other at amortised cost are initially recognised at fair value, which is typically equal to cost, i.e. cash advanced less any transaction costs. They are subsequently measured at amortised cost using the effective interest method. Accrued interest, in the case of interest bearing liabilities is included in the carrying amount. Interest expense is recognised in net interest expense.

Notes

11. Determination of fair value

The determination of fair value of financial assets and financial liabilities that are quoted in an active market is based on quoted prices. A market is considered active if quoted prices are readily and regularly available and those prices represent actual and regularly occurring market transactions on an arm's length basis. For all other financial instruments fair value is determined by using valuation techniques.

Valuation techniques include recent arm's length transactions between knowledgeable, willing parties, if available, reference to the current fair value of other instruments that are substantially the same, the discounted cash flow analysis and option pricing models. Valuation techniques incorporate all factors that market participants would consider in setting a price and are consistent with accepted methodologies for pricing financial instruments. Periodically, the Bank calibrates the valuation technique and tests it for validity using prices from any observable current market transactions in the same instrument, without modification or repackaging, or based on any available observable market data.

For more complex instruments, the Bank uses proprietary models, which usually are developed from recognised valuation models. Some or all of the inputs into these models may not be market observable, and are derived from market prices or rates or are estimated based on assumptions. When entering into a transaction, the financial instrument is recognised initially at the transaction price, which is the best indicator of fair value, although the value obtained from the valuation model may differ from the transaction price. This initial difference, usually an increase in fair value, indicated by valuation techniques is recognised in income depending upon the individual facts and circumstances of each transaction and no later than when the market data becomes observable.

The value produced by a model or other valuation technique is adjusted to allow for a number of factors as appropriate, because valuation techniques cannot appropriately reflect all factors market participants take into account when entering into a transaction. Valuation adjustments are recorded to allow for model risks, bid-ask spreads, liquidity risks, as well as other factors. Management believes that these valuation adjustments are necessary and appropriate to fairly state financial instruments carried at fair value in the statement of financial position.

12. Impairment

a. General principle

The carrying amount of the Bank's financial assets not at fair value through profit and loss is reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. An impairment is recognised in the income statement whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount.

b. Reversal of impairment

If, in a subsequent period, the amount of an impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is recognised as reduction of cost in the income statement.

c. Calculation of recoverable amount

The recoverable amount of the Bank's investments in financial assets carried at amortised cost is calculated as the present value of estimated future cash flows, discounted at the original effective interest rate.

The recoverable amount of other assets is the greater of their fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

13. Impairment of loans

a. Indications of impairment

Objective evidence of impairment includes information about one or more of the following:

- Indications of significant financial difficulties of the borrower, including financial restructuring and refinancing concessions that a lender would not otherwise consider
- A breach of contract, such as a default on installments or on interest or principal payments
- An observable decrease in the estimated future cash flows from a group of loans due to adverse changes in the economic conditions of a sector or region in which the borrower operates, even if the decrease cannot yet be identified with the individual financial assets in the group
- The disappearance of an active market for an asset held as collateral

Impairment losses expected as a result of events taking place after the reporting date, no matter how likely, are not recognised.

b. Calculation of impairment losses

Impairment loss is calculated by comparing the carrying amount of individual loans with the present value of their expected future cash flows, discounted at their original effective interest rate. In the case of loans at variable interest rates, the discount rate used is their current effective interest rate.

Notes

c. Individually assessed loans

Impairment losses on individually assessed loans are determined by an evaluation of the exposures on a case-by-case basis. This procedure is applied to all loans that are considered individually significant. In making the assessment, the following factors are considered:

- The Bank's aggregate exposure towards the customer
- The amount and timing of expected receipts and recoveries
- The likely dividend available on liquidation or bankruptcy
- Complexity and uncertainty related to ranking of creditor claims and legal standing
- The realisable value of securities or other credit mitigants and the likelihood of successful reposession
- The likely deduction of any costs involved in recovery of amounts outstanding

d. Collectively assessed loans

Impairment losses on collectively assessed loans are determined by an evaluation of the exposures on a group of loans with similar risk characteristics. This procedure is applied to all loans that are not considered individually significant, or have been individually assessed but showed no indications of impairment. This loss covers loans that are impaired at the reporting date but which will not be individually identified as such until some time in the future.

The collective impairment loss is determined after taking into account the following:

- Historical loss experience in portfolios of similar risk characteristics, for example, by industry sector, loan grade or product
- The estimated period between a loss occurring and that loss being identified and evidenced by the establishment of an allowance against the loss on an individual loan
- Management's experienced judgement as to whether the current economic and credit conditions are such that the actual level of inherent losses is likely to be greater or less than that suggested by historical experience

Estimates of changes in future cash flows for groups of assets are consistent with changes in observable data from period to period, for example changes in property prices, payment status, or other factors indicative of changes in the probability of losses on the group and their magnitude. The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Bank to minimise any differences between loss estimates and actual losses.

e. Loan write-offs

The carrying amount of impaired loans is reduced through the use of an allowance account. Loans are written off, partially or in full, when there is no realistic prospect of recovery.

14. Share capital

a. Treasury shares

Acquired own shares and other equity instruments (treasury shares) are deducted from equity. No gain or loss is recognised in income statement on the purchase, sale, issue or cancellation of treasury shares. Consideration paid or received is recognised directly in equity. Incremental transaction costs of treasury share transactions are accounted for as a deduction from equity, net of any related income tax benefit.

b. Share premium

Share premium represents excess of payment above nominal value (ISK 1 per share) that shareholders have paid for shares sold by the Bank. According to Icelandic Companies Act, 25% of the nominal value of share capital must be held in reserve which can not be paid out as dividend to shareholders.

c. Dividends on share capital

Dividends on share capital are deducted from equity in the period in which they are approved by the Bank's shareholders meetings.

15. Interest income and expense

Interest income and expense are recognised in the income statement using the effective interest method. The effective interest rate is the rate that exactly discounts estimated future cash flows to the carrying amount of the financial asset or liability, over the the expected life of the financial instrument. Estimated future cash flows take into account all contractual terms of the financial instruments but not future credit losses.

Interest income and expense presented in the income statement includes interest on:

- financial assets and liabilities classified as loans and receivables
- financial assets and liabilities carried at amortised cost
- financial assets and liabilities classified as held to maturity
- financial assets classified as available for sale
- derivatives

Further information about the accounting classification of financial assets and liabilities is provided in note 10.

Notes

16. Fee and commission income and expense

The Bank earns income from providing various services to its customers. This includes fees for managing assets on behalf of customers, commissions received for equity and bond transactions and fees and commissions for various other financial services.

- Fee and commission income and expenses that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate
- Other fee and commission income is recognised in the income statement as the services are provided
- Fee and commission expense relates mainly to transaction fees, which are expensed as the services are received

17. Net financial income

Net financial income comprises the following:
- Realised and unrealised gains or losses from price changes of fixed income securities carried at fair value
- Realised and unrealised gains or losses from price changes of variable income securities
- Interest income from fixed income securities carried at fair value
- Dividends, excluding dividends from associates and subsidiaries
- Foreign exchange difference

18. Dividend income

Dividend income is recognised when the right to receive income is established. Usually this is the ex-dividend date for equity securities. Dividends, other than those from associates and subsidiaries, are reflected as component of net financial income.

19. Administrative expenses

Administrative expenses comprise expenses other than interest expenses, fee and commission expenses and expenses related to fair value changes. A breakdown of administrative expenses is provided in note 62.

20. Employee benefits

Contractual payments to contribution pension plans are recognised as an expense in profit or loss when they are due. The Bank has no further obligations once those contributions have been paid.

21. Income tax

Income tax comprises current and deferred tax. Income tax is recognised in the income statement, except to the extent that it relates to items recognised directly in other comprehensive income or equity, in which case it is recognised there.

Current tax liabilities include the estimated tax payable next year on current year's profit according to the tax rates prevailing at reporting date, in addition to corrections on tax from previous years and unpaid taxes from the previous year, if any.

The deferred income tax asset and/or liability has been calculated and recognised in the statement of financial position. The calculation is based on the difference between assets and liabilities as presented in the tax return on one hand, and in the consolidated financial statements on the other, taking into consideration tax losses carried forward. This difference is due to the fact that the tax assessment is based on premises that differ from those governing the financial statements, mostly due to temporary differences arising from the recognition of revenue and expense in the tax returns and in the financial statements.

Deferred tax assets and tax liabilities are are offset in the statement of financial position when there is a legal right to settle on a net basis and they are levied by the same taxing authority on the same entity or on different entities subject to joint taxation.

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 reduced to the extent that it is no longer probable that the related tax benefit will be realised.

22. Cash and cash equivalents

Cash and cash equivalents comprise balances with less than three months maturity from the date of acquisition, including cash in hand, balances with banks, unrestricted balances with Central Bank and other short-term highly liquid investments with original maturities of three months or less.

Notes

23. Fixed income securities

Fixed income securities are initially measured at fair value and subsequently accounted for depending on their classification as discussed in note 10.

24. Shares and other variable income securities

Shares and other variable income securities consist of equity investments and unit shares in mutual funds. Shares and other variable income securities are initially measured at fair value and subsequently accounted for depending on their classification as discussed in note 10.

25. Securities used for hedging

Securities used for hedging consist of non-derivative financial assets that are used to hedge the Bank's risk exposure arising from derivative contracts with customers. Securities used for hedging are designated at fair value as discussed in note 10.

26. Loans to customers

Loans are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and include loans provided by the Bank to its customers, participation in loans from other lenders and purchased loans that are not quoted in an active market and which the Bank has no intention of selling immediately or in the near future.

Loans are initially recognised at fair value, which is the cash advanced, plus any transaction costs. Subsequently, they are measured at amortised cost using the effective interest method. Accrued interest is included in the carrying amount of the loans and advances. The carrying amount of impaired loans is reduced through the use of an allowance account.

When the Bank purchases a financial asset and simultaneously enters into an agreement to resell the asset, or a substantially similar asset, at a fixed price at a future date (“reverse repo” or “stock borrowing”), the arrangement is accounted for as a loan and the underlying asset is not recognised in the Bank’s statement of financial position.

27. Derivatives

A derivative is a financial instrument or another contract that falls under the scope of IAS 39 and has the following three characteristics:
- Its price changes due to changes in an underlying variable, such as bond price, share price, security or price index (including CPI), foreign currency exchange rate or interest rate
- The contract requires no initial investment or an initial investment that is smaller than would be required for a non-derivative contract with the same sensitivity to market change
- Settlement takes place at a future date

The Bank uses derivatives for trading purposes and to hedge its exposure to market price risk, foreign exchange risk and inflation and interest risk arising from operating, financing and investing activities. The Bank does not use hedge accounting.

Derivative assets and liabilities are initially recognised and subsequently measured at fair value in the statement of financial position. Derivatives with positive fair values are classified as financial assets and deratives with negative fair values as financial liabilities. Revenue from derviatives is split into interest income and net income from financial instruments at fair value and presented in the corresponding line items in the income statement.

28. Intangible assets

a. Asset categories
The Bank groups intangible assets into three categories:

- Software
  Software comprise acquired software licences and external costs associated with the development of bespoke applications.
- Goodwill
  Goodwill arises in business combinations and equals the difference between the purchase price and share in the net assets of the acquired company. Net assets include book equity and the revaluation of assets and liabilites, if relevant, and the value of off-balance sheet assets and liabilities. Following initial recognition, goodwill is recognised at cost, less impairment.
- Other intangible assets
  Other intangible assets comprise licences and acquired trademarks used in the operation of the Bank.

Notes

b. Initial recognition
Intangible assets are initally recognised at cost.

c. Subsequent measurement
The Bank uses the cost model for measurement after recognition and intangible assets are carried at cost less accumulated amortization and impairment. Intangible assets are reviewed for indications of impairment or changes in estimated future economic benefits at each reporting date. If such indications exist, the assets are analysed to assess whether their carrying amount is fully recoverable. An impairment loss is recognized if the carrying amount exceeds the recoverable amount.

d. Amortization
Intangible assets with finite useful life are amortized using the straight-line method over their estimated useful economic life, with the amortization recognised in the income statement. The estimated useful life of intangible assets is as follows:

Software	5-10 years
Other intangible assets with finite useful life	10 years

29. Property and equipment

a. Asset categories
The Bank groups intangible assets into two categories:

- Real estate
  Real estate comprise office buildings and sub-units.
- Other property and equipment
  Other property and equipment comprise automobiles, furniture and fixtures, computers and other office equipment.

b. Initial recognition
Property and equipment is initially recognised at cost, which includes direct expenses related to the purchase.

c. Subsequent measurement
The Bank uses the cost model for the measurement after recognition and property and equipment is carried at cost less accumulated depreciation and impairment. Property and equipment is reviewed for indications of impairment or changes in estimated future economic benefits at each reporting date. If such indications exist, the assets are analysed to assess whether their carrying amount is fully recoverable. An impairment loss is recognized if the carrying amount exceeds the recoverable amount.

d. Subsequent cost
The Bank recognises in the carrying amount of an item of property and equipment the cost of replacing part of such an item when that cost is incurred if it is probable that the future economic benefits embodied with the item will flow to the Bank and the cost of the item can be measured reliably. The decision, if subsequent costs are added to the acquisition cost of property and equipment, is based on whether an identified component, or part of such component, has been replaced or not, or if the nature of the subsequent cost means a contribution of a new component. All other costs are expensed in the income statement when incurred.

e. Depreciation
Depreciation is recognised in the income statement on a straight-line basis over the estimated useful lives of each component of an item of property and equipment. The estimated useful lives are as follows:

Real estate	15-50 years
Other property and equipment	3-5 years

Where parts of an item of property and equipment have different useful lives, those components are accounted for separately.

30. Other assets

Other assets are measured at cost.

31. Deposits

Deposits consist of time deposits and demand deposits. Money market deposits are included in borrowings. Deposits are recognised at amortized cost, including accrued interest.

Notes

32. Borrowings

Borrowings are initially recognised at fair value less attributable transaction costs. Subsequently, they are measured at amortized cost using the effective interest method. Accrued interest is included in their carrying amount.

When the Bank sells a financial asset and simultaneously enters into an agreement to repurchase the asset, or a substantially similar asset, at a fixed price at a future date (“repo” or “stock lending”), the arrangement is accounted for as a borrowing and the underlying asset continues to be recognised in the Bank’s statement of financial position.

33. Short positions in securities

Short positions are carried at fair value with all fair value changes recognised in the income statement under net financial income.

34. Short positions in securities used for hedging

Short positions in securities used for hedging consist of non-derivative financial liabilities that are used to hedge the Bank's risk exposure arising from derivative contracts with customers. Short positions in securities used for hedging are designated at fair value as discussed in note 10.

35. Other liabilities

Other liabilities are measured at cost.

36. New standards and interpretations

A number of new standards, amendments to standards and interpretations are not yet effective for the current financial year and have not been applied in preparing these financial statements. None of them will have material effect on the financial statements with the possible exeption of IFRS 9 Financial instruments, which, if endorsed by the EU, will be mandatory for the Bank for the first time for the year 2015. Its adoption can affect the classification and valuation of financial assets and financial liabilities. Early adoption of the standard is not planned and the effects of the adoption have not been estimated.

37. Use of estimates and judgement

The Bank makes estimates and assumptions that affect the reported amounts of assets and liabilities within the financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

a. Impairment losses
As outlined in notes 12 and 13, the use of estimates and judgement is an important component of the calculation of impairment losses. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience. Unforeseen events could, however, result in further impairment losses which would have a material effect on the income statement and statement of financial position.

b. Deferred tax asset
The value of a deferred tax asset is estimated by management, based on projections about future profits and the extent to which the tax asset will be realised.

c. Fair value of financial instruments
The fair value of financial instruments that are not quoted in active markets is determined using valuation techniques which are reviewed regularly by qualified independent personnel. All models that are used must be approved and calibrated to ensure that outputs reflect actual data.

Notes

Risk management

38. Risk management disclosure

a. Committees

The Bank operates three committees that are involved in risk management: an Asset and Liability Committee (ALCO), a Credit Committee and a Quality and Security Committee.

The ALCO committee meets regularly and each department reports on its operations and positions activity since the previous meeting. The committee addresses matters regarding the Bank's risk management, financing, capital management and proprietary trading.

The Credit Committee addresses matters regarding the Bank's loan activities. The committee is responsible for the approval of individual loans as well as deciding on credit limits for individual clients in derivative trades, and is the primary forum for the discussion of loan activity policy.

The Quality and Security Committee is responsible for supervision and implementation of the Bank’s security and quality policies. The security policy mainly addresses data security and operational security in IT systems, physical security for the personnel and proper access controls and monitoring in the Bank‘s premises. The quality work is aimed at upholding proper quality in work processes, IT systems and services to support performance and profitability, lower operational risk and increase the customer experience.

b. Risk management and credit control unit

The purpose of the risk management and credit control unit is to identify, quantify, control and report on the risks that the Bank is exposed to in its daily activities. The unit also participates in drafting the overall risk policy of the Bank and has representatives on the ALCO committee and the Quality and Security committee. The unit’s main activities include monitoring and managing credit risk, market risk, liquidity risk and operational risk. The board of directors sets the rules and guidelines regarding the Bank's risk policy and the obligations of risk management and credit control. The division reports regularly on the Bank’s positions and exposure to risk to the board of directors, the CEO and to the ALCO committee.

c. Internal auditor

Internal auditor has the role to give objective opinon on the Bank's operations and advisory that aims to increase its value, and to strengthen risk management and control. The tasks of internal audit and main emphasis are to estimate whether processes and systems are in place, and whether they are relevant and efficient. Internal auditor is recruited by the board and is located accordingly in the hierarchy. It's operations cover all units of operations, including subsidiaries.

39. Hedging

A part of the Bank’s portfolio consists of securities held as a hedge against derivatives positions of customers. The Bank hedges currency exposure between the Bank's loan portfolio and debts to the extent possible, but does not use hedge accounting.

Notes

40. Credit risk - overview

a. Definition

One of the Bank’s primary sources of risk is counterparty credit risk. If one or more counterparties, typically borrowers, fail to meet their financial obligations towards the Bank, the Bank has to recognise losses due to these defaults.

b. Management

The risk management and credit control unit is responsible for managing and reporting on credit risk. The Bank uses a variety of tools and processes to manage credit risk, including collaterals, hedges and loan portfolio management.

c. Credit approval process

The originating department prepares a proposal for each loan or credit line which is presented to the credit committee for approval. The proposal consists of a basic description of the client, the purpose of the loan, a simple credit assessment and arguments for or against granting the loan. The committee decides whether there is need for further credit assessment and on what terms the loan may be granted.

A more thorough credit assessment may be conducted if considered appropriate and can include an assessment of a borrower’s fundamental credit strength as well as the value of any collateral. To assess the borrower’s capacity to meet his or her obligations the committee can request stress test analysis of the borrower’s cash flow or call for third party assessments.

d. Credit collateral

Securing loans with collateral is a traditional method to reduce credit risk. The Bank uses different methods to reduce credit risk by obtaining collateral from customers where appropriate. Such collateral gives the Bank right to the collateralised assets for current and future obligations incurred by the customer.

The Bank places emphasis on ensuring that loans are secured with collateral that can be marked to market, and that asset coverage exceeds 100%. The Bank applies appropriate haircuts on all collateral in listed securities in order to ensure proper risk mitigation. For all collateral in listed securities, the Bank maintains the right to liquidate collateral in case its market value falls below a predefined limit.

To a very large extent the Bank’s loan portfolio consists of senior loans, most of which are highly collateralised.

e. Credit rating, control and provisioning

The risk management and credit control unit is responsible for credit rating and reviewing the loan portfolio. In case of any significant delay of payments or defaults the unit carefully analyses the underlying assets and loan documents and organizes the process of collection.

The Bank monitors the value of collateral by listed securities on a real time basis, and takes prompt action when necessary.

Provisioning for loan impairments is estimated on the basis of models assessing a portfolio as a whole based on the seniority of the loans, the degree of collateralisation and the Bank's history of defaulted loans. Risk management and credit control suggest a provisioning percentage for the portfolio, based on the expected loss assessment. Risk management and credit control reassess impairments in the event of collateral decay, delayed payments or other early warning signs. Provisions require approval by the CEO and the credit committee.

f. Loan portfolio management

To ensure an effective diversification of the loan portfolio the board has set a limit framework defining maximum exposure as a ratio of the Bank’s equity and/or the total size of the loan portfolio. These limits include limitation on joint exposure to associated clients, exposure to individual and associated industries, single regions and countries etc. It is the responsibility of risk management and credit control to monitor that these limits are not being violated and to report discrepancies to the credit committee.

g. Derivatives

The Bank offers derivative contracts in the form of swap contracts on listed, highly liquid securities. On the day when the contract is entered into, the Bank purchases the underlying security and hedges its exposure to price changes. Collateral is in the form of cash or listed, highly liquid securities. The Bank's risk management sets rules about the level of collateralisation and monitors the compliance to these rules. Contracts are closed if required levels of collateralisation are not met.

h. Securities used for hedging

The Bank hedges itself for market risk of derivative contracts by purchasing the underlying securities at the commencement of the contract. Since the contracts require delivery of the underlying securities to the customer on the settlement day, the credit risk towards the issuer is immaterial.

MP Bank hf. Amounts are in ISK thousands

Notes

41. Maximum exposure to credit risk

The maximum exposure to credit risk of on-balance sheet and off-balance sheet financial instruments, before taking into account any collateral held or other credit enhancements, is specified as follows:

	30.9.2012	31.12.2011
Cash and cash equivalents	29,583,967	11,545,143
Receivables from Central Bank	8,309,760	0
Fixed income securities	5,606,042	13,678,864
Shares and other variable income securities	607,421	583,654
Securities used for hedging	200,000	6,967,719
Loans to customers	23,611,085	13,294,303
Derivatives	233,806	199,571
Other assets	511,698	662,246
	68,663,779	46,931,500
Loan committments	4,578,492	6,046,285
Financial guarantee contracts	769,092	159,648
Total	74,011,362	53,137,433

42. Financial assets not measured at fair value - credit risk

Financial assets not measured at fair value, but exposed to credit risk, are specified as follows:

30.9.2012	Neither past due nor individually impaired	Past due but not individually impaired	Individually impaired	Claim value	Less specific impairment allowance	Less collective impairment allowance	Net carrying amount
Cash and cash equivalents	29,583,967			29,583,967			29,583,967
Receivables from Central Bank	8,309,760			8,309,760			8,309,760
Loans to customers	23,143,792	403,058	517,954	24,064,804	(317,852)	(135,867)	23,611,085
Other assets	511,698			511,698			511,698
Total	61,549,217	403,058	517,954	62,470,228	(317,852)	(135,867)	62,016,510

31.12.2011	Neither past due nor individually impaired	Past due but not individually impaired	Individually impaired	Claim value	Less specific impairment allowance	Less collective impairment allowance	Net carrying amount
Cash and cash equivalents	11,545,143			11,545,143			11,545,143
Fixed income securities	9,245,989			9,245,989			9,245,989
Loans to customers	12,689,381	494,883	318,436	13,502,700	(152,467)	(55,929)	13,294,303
Derivatives				0			0
Other assets	662,246			662,246			662,246
Total	34,142,758	494,883	318,436	34,956,078	(152,467)	(55,929)	34,747,681

Past due but not impaired financial assets are those assets where contractual payments are more than 30 days past due but the Bank believes that impairment is not appropriate on the basis of the level of security, or future cash flows of the borrower. Past due loans are reported as the total claim value and not only those payments that are past due.

MP Bank hf. Amounts are in ISK thousands

Notes

43. Breakdown of loans

a. By segments

The breakdown of the loan portfolio by industries is specified as follows:

	30.9.2012	%	31.12.2011	%
Services	7,795,423	33.0%	4,964,494	37.3%
Holding companies	3,850,765	16.3%	3,013,221	22.7%
Individuals	5,649,295	23.9%	2,577,154	19.4%
Other	6,315,603	26.7%	2,739,434	20.6%
Total	23,611,085	100.0%	13,294,303	100.0%

b. By seniority

The Bank’s loan portfolio mainly consists of senior I loans which are secured with collateral which can be marked to market, and have asset coverage exceeding 100% and senior II loans which have first priority claims on the borrower’s assets, and in some cases collateral such as unlisted shares and other collateral which cannot be marked to market. The loan portfolio contains less than 25% of junior loans which have second line claims on the borrower’s assets and loans where the loan is unsecured and subordinated to all of the borrower’s liabilities.

44. Foreclosed assets

The Bank's policy is to sell foreclosed assets as soon as possible. These assets are not shown separately in the Bank's accounts but included among other comparable assets. The Bank did not take possession of collateral held as security in 2012 or 2011.

45. Large exposures

In accordance with the Financial Supervisory Authority's regulation no. 216/2007 on financial institutions' large exposures, total exposure towards a customer is classified as a large exposure if it exceeds 10% of the Bank's capital base (see note 83). According to the regulation a single exposure, net of collateralised assets, cannot exceed 25% of the capital base.

	30.9.2012		31.12.2011	
Large exposures net of collateralised assets	**Number**	**Amount**	**Number**	**Amount**
10-20% of capital base	5	2,233,930	3	1,627,123
20-25% of capital base	0	0	0	0
Exceeding 25% of capital base	0	0	0	0
Total	5	2,233,930	3	1,627,123

Amounts are in ISK thousands

Notes

46. Liquidity risk

a. Definition

Liquidity risk is the risk that the Bank will encounter difficulty in meeting contractual payment obligations associated with its financial liabilities, or will only be able to do so substantially above the prevailing market cost of funds. This risk mainly arises from mismatches in the timing of cash flows. The Bank has internal rules that require certain matching of the maturities of assets and liabilities. Furthermore, to ensure the sufficiency of funds, the Bank has lines of credit, overdraft facilities and highly liquid securities such as treasury bills and treasury bonds.

b. Management

Liquidity is managed by treasury and monitored by risk management. Liquidity position is reported to the ALCO comittee. The Bank is subject to the Central Bank's requirements about minimum coverage ratio between cash flows of assets and liabilities. The Bank was in compliance with external liquidity requirements throughout the period.

c. Breakdown of financial assets and financial liabilities by maturity

The table below shows the contractual maturity of financial assets and liabilities, for both on-balance sheet and off-balance sheet items. The analysis is based on contractual maturity in accordance with IFRS 7. The table does not take future interest payments into account and therefore doesn't fully reflect future cash flows.

Furthermore, since the table is based on contractual maturities it doesn't reflect the liquid nature of market securities which can be converted to cash through repo transactions. Such securities amounted to ISK 1.3 billion on the reporting date and could be converted to cash within two days.

Financial assets 30.9.2012	**0-1 months**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**No stated maturity**	**Total**
Cash and cash equivalents	29,583,967						29,583,967
Receivables from Central Bank	8,309,760						8,309,760
Fixed income securities			110,338	1,959,066	3,512,191	24,447	5,606,042
Shares and other variable income securities						1,080,460	1,080,460
Securities used for hedging					200,000	1,528,625	1,728,625
Loans to customers	5,472,238		6,521,745	7,534,031	4,083,071		23,611,085
Other assets	52,825	99,097	194,212			165,565	511,698
Financial assets excluding derivatives	43,418,790	99,097	6,826,294	9,493,097	7,795,262	2,799,097	70,431,638
Derivatives	121,025	28,597		84,185			233,806
Total	43,539,815	127,693	6,826,294	9,577,282	7,795,262	2,799,097	70,665,444

Financial liabilities 30.9.2012	**0-1 months**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**No stated maturity**	**Total**
Deposits	36,092,925	1,208,695	5,688,178	1,314,792	64,819		44,369,409
Borrowings	9,165,158						9,165,158
Short positions in securities			3,683,093	242,714	938,238	241	4,864,286
Short positions in securities used for hedging ..			947,081	954,232	2,118,843		4,020,156
Other liabilities	4,883,875	119,390	160,854				5,164,119
Financial liabilities excluding derivatives	50,141,957	1,328,085	10,479,206	2,511,738	3,121,900	241	67,583,128
Derivatives	90,529	28,476			2,240		121,245
Total	50,232,486	1,356,562	10,479,206	2,511,738	3,124,140	241	67,704,373

30.9.2012	**0-1 months**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**No stated maturity**	**Total**
Financial assets	43,539,815	127,693	6,826,294	9,577,282	7,795,262	2,799,097	70,665,444
Financial liabilities	(50,232,486)	(1,356,562)	(10,479,206)	(2,511,738)	(3,124,140)	(241)	(67,704,373)
Loan committments	(1,084,339)	(778,420)	(1,754,652)	(942,219)	(18,862)		(4,578,492)
Financial guarantee contracts	(42,486)	(231,513)	(238,585)	(230,336)	(26,172)		(769,092)
Net financial assets (liabilities)	(7,819,496)	(2,238,801)	(5,646,148)	5,892,989	4,626,087	2,798,856	(2,386,512)

MP Bank hf. Amounts are in ISK thousands

Notes

Financial assets 31.12.2011	0-1 months	1-3 months	3-12 months	1-5 years	Over 5 years	No stated maturity	Total
Cash and cash equivalents	11,545,143						11,545,143
Fixed income securities	306,685	102,861	53	513,267	12,755,288	711	13,678,864
Shares and other variable income securities						1,068,531	1,068,531
Securities used for hedging				269,794	6,656,888	768,155	7,694,837
Loans to customers	5,610,944		3,354,010	3,042,327	1,287,022		13,294,303
Other assets	411,816	26,845	20,320			203,264	662,246
Financial assets excluding derivatives	17,874,589	129,705	3,374,383	3,825,388	20,699,198	2,040,661	47,943,925
Derivatives	101,183	10,686	87,702				199,571
Total	17,975,772	140,391	3,462,085	3,825,388	20,699,198	2,040,661	48,143,496

Financial liabilities 31.12.2011	0-1 months	1-3 months	3-12 months	1-5 years	Over 5 years	No stated maturity	Total
Deposits	28,043,037	2,870	4,626,824	1,868,469	52,883		34,594,083
Borrowings	2,051,155						2,051,155
Short positions in securities			3,801,395	530,866	506,261	442	4,838,963
Short positions in securities used for hedging			458,543	815,686			1,274,229
Other liabilities	1,721,122	226,766	199,318				2,147,207
Financial liabilities excluding derivatives	31,815,314	229,636	9,086,080	3,215,021	559,144	442	44,905,637
Derivatives	94,465	7,033					101,498
Total	31,909,779	236,669	9,086,080	3,215,021	559,144	442	45,007,135

31.12.2011	0-1 months	1-3 months	3-12 months	1-5 years	Over 5 years	No stated maturity	Total
Financial assets	17,975,772	140,391	3,462,085	3,825,388	20,699,198	2,040,661	48,143,496
Financial liabilities	(31,909,779)	(236,669)	(9,086,080)	(3,215,021)	(559,144)	(442)	(45,007,135)
Loan committments	(699,346)		(4,442,079)	(669,036)	(235,824)		(6,046,285)
Financial guarantee contracts	(8,819)	(48,057)	(49,525)	(47,813)	(5,433)		(159,648)
Net financial assets (liabilities)	(14,642,172)	(144,336)	(10,115,599)	(106,483)	19,898,798	2,040,220	(3,069,572)

MP Bank hf. Amounts are in ISK thousands

Notes

47. Currency risk

a. Definition

Currency risk arises when financial instruments are not denominated in the reporting currency and can both affect the Bank's income statement and statement of financial position. A substantial part of the Bank's financial assets and liabilities is denominated in foreign currencies.

b. Management

Currency positions are monitored by risk management and reported to the ALCO committee. Any mismatch between assets and liabilities in each currency is monitored closely and managed within limits.

The Bank is subject to limits set by the Central Bank of Iceland regarding the maximum open currency position. At 30 September 2012 the Bank's position in foreign currencies was within those limits.

c. Exchange rates

The following exchange rates have been used by the Bank in the preparation of the financial statements:

	30.9.2012	31.12.2011	Average 9m 2012	Average 2011
EUR/ISK	160.0	158.8	159.8	161.5
LTL/ISK	46.3	46.0	46.6	46.8
NOK/ISK	21.7	20.4	21.3	20.7
USD/ISK	123.7	122.7	124.7	116.0
ISK trade index	202.3	204.9	208.2	204.5

d. Breakdown of financial assets and financial liabilities denominated in foreign currencies, by currency

Financial assets 30.9.2012	**EUR**	**LTL**	**NOK**	**USD**	**Other currencies**	**Total**
Cash and cash equivalents	2,142,964	131,059	110,692	1,250,946	448,842	4,084,504
Fixed income securities		24,447	108,978			133,425
Shares and other variable income securities	770			84,377	72,200	157,348
Securities used for hedging	93,129		1,440	2,569		97,138
Loans to customers	1,009,392		109,385	835,900	21,576	1,976,254
Other assets		251,690		72,783		324,473
Financial assets excluding derivatives	3,246,256	407,196	330,495	2,246,575	542,619	6,773,141
Derivatives	32,407		1,235	5,904		39,546
Total	3,278,662	407,196	331,731	2,252,479	542,619	6,812,687

Financial liabilities 30.9.2012	**EUR**	**LTL**	**NOK**	**USD**	**Other currencies**	**Total**
Deposits	3,294,651		211,934	1,506,100	500,284	5,512,969
Short positions in securities			16	225		241
Financial liabilities excluding derivatives	3,294,651	0	211,950	1,506,325	500,284	5,513,210
Derivatives				173,124		173,124
Total	3,294,651	0	211,950	1,679,449	500,284	5,686,334

Net currency position 30.9.2012	**EUR**	**LTL**	**NOK**	**USD**	**Other currencies**	**Total**
Financial assets	3,278,662	407,196	331,731	2,252,479	542,619	6,812,687
Financial liabilities	(3,294,651)		(211,950)	(1,679,449)	(500,284)	(5,686,334)
Net off-balance sheet position	(132,256)			(237,759)	(88,314)	(458,329)
Total	(148,244)	407,196	119,781	335,271	(45,980)	668,024

MP Bank hf. Amounts are in ISK thousands

Notes

Financial assets 31.12.2011	EUR	LTL	NOK	USD	Other currencies	Total
Cash and cash equivalents	514,552	13,538	93,804	625,072	206,039	1,453,006
Fixed income securities	320,486	711	102,861			424,058
Shares and other variable income securities	715	2		66,282	89,172	156,171
Securities used for hedging	107,635		1,053	2,637		111,325
Loans to customers	638,725	343,534		882,338	217,970	2,082,567
Financial assets excluding derivatives	1,582,113	357,786	197,718	1,576,328	513,181	4,227,126
Derivatives	51,407		4,448	934,025		989,880
Total	1,633,520	357,786	202,166	2,510,353	513,181	5,217,005

Financial liabilities 31.12.2011	EUR	LTL	NOK	USD	Other currencies	Total
Deposits	1,986,875		194,448	1,715,391	135,883	4,032,596
Short positions in securities	6		128	307		442
Financial liabilities excluding derivatives	1,986,881	0	194,576	1,715,698	135,883	4,033,037
Derivatives	317,680			306,775	159,021	783,476
Total	2,304,561	0	194,576	2,022,473	294,904	4,816,513

Net currency position 31.12.2011	EUR	LTL	NOK	USD	Other currencies	Total
Financial assets	1,633,520	357,786	202,166	2,510,353	513,181	5,217,005
Financial liabilities	(2,304,561)		(194,576)	(2,022,473)	(294,904)	(4,816,513)
Net off-balance sheet position						0
Total	(671,041)	357,786	7,589	487,880	218,277	400,492

e. Sensitivity to currency risk

Given the net currency position, a 10% change in the value of the ISK would, with other things constant, result in the following changes to the Bank's pre-tax profit.

	30.9.2012		31.12.2011	
Assets and liabilities denominated in	**-10%**	**+10%**	**-10%**	**+10%**
EUR	(14,824)	14,824	(67,104)	67,104
LTL	40,720	(40,720)	35,779	(35,779)
NOK	11,978	(11,978)	759	(759)
USD	33,527	(33,527)	48,788	(48,788)
Other currencies	(4,598)	4,598	21,828	(21,828)
Total	66,802	(66,802)	40,049	(40,049)

The effect on equity would be the same, net of income tax.

MP Bank hf. Amounts are in ISK thousands

Notes

48. Interest rate risk

a. Definition

The Bank's exposure to interest rate risk is twofold. On one hand, the Bank has a proprietary portfolio of bonds, where market rates affect prices and any fluctuations are recognised in the income statement. On the other hand, the Bank has mismatch in assets and liabilities with fixed interest terms in the banking book. The banking book generally pertains to the Bank's loans and swap contracts for securities on the asset side and borrowings and deposits on the liability side. This mismatch does not create an immediate effect on the income statement but nevertheless affects the Bank's economic value.

Proprietary positions which are subject to interest rate risk fall under the scope of the Bank's market risk management.

b. Management

The Bank takes measures to minimise interest rate risk in the banking book by matching the interest rate profile and duration of assets with the Bank's liabilities. This is obtained in part by matching the currency and duration of the funding of the Bank with its assets, as well as using derivative and non-derivative financial instruments to manage effectively the risk of an adverse impact on the Bank's earnings.

c. Breakdown of financial assets and financial liabilities by currency and interest repricing time

The breakdown of financial assets and liabilities by currency and the earlier of interest repricing time or maturity is specified as follows:

Financial assets						**Other**	
30.9.2012	**ISK**	**EUR**	**DKK**	**NOK**	**USD**	**currencies**	**Total**
0-1 year	21,542,176	930,730	21,459	113,013	618,083		23,225,461
1-2 years	437,582						437,582
2-3 years	2,830,289						2,830,289
3-4 years	5,982						5,982
Over 4 years	1,223,565						1,223,565
Total	26,039,594	930,730	21,459	113,013	618,083	0	27,722,879

Financial liabilities						**Other**	
30.9.2012	**ISK**	**EUR**	**DKK**	**NOK**	**USD**	**currencies**	**Total**
0-1 year	56,036,155	3,294,651	237,606	211,934	1,506,100	262,678	61,549,124
Total	56,036,155	3,294,651	237,606	211,934	1,506,100	262,678	61,549,124

Net imbalance						**Other**	
30.9.2012	**ISK**	**EUR**	**DKK**	**NOK**	**USD**	**currencies**	**Total**
0-1 year	(34,493,979)	(2,363,920)	(216,147)	(98,921)	(888,018)	(262,678)	(38,323,663)
1-2 years	437,582						437,582
2-3 years	2,830,289						2,830,289
3-4 years	5,982						5,982
Over 4 years	1,223,565						1,223,565
Total	(29,996,561)	(2,363,920)	(216,147)	(98,921)	(888,018)	(262,678)	(33,826,246)

MP Bank hf. Amounts are in ISK thousands

Notes

Financial assets 31.12.2011	ISK	EUR	LTL	NOK	USD	Other currencies	Total
0-1 year	18,921,570	444,586			7,999	3,753	19,377,908
1-2 years	1,750				636,619		638,369
2-3 years	2,000,000						2,000,000
3-4 years	4,400						4,400
Over 4 years	10,034,515						10,034,515
Total	30,962,235	444,586	0	0	644,618	3,753	32,055,192

Financial liabilities 31.12.2011	ISK	EUR	LTL	NOK	USD	Other currencies	Total
0-1 year	36,942,807	1,979,494			1,708,091	330,070	40,960,463
Total	36,942,807	1,979,494	0	0	1,708,091	330,070	40,960,463

Net imbalance 31.12.2011	ISK	EUR	LTL	NOK	USD	Other currencies	Total
0-1 year	(18,021,237)	(1,534,908)			(1,700,093)	(326,317)	(21,582,555)
1-2 years	1,750				636,619		638,369
2-3 years	2,000,000						2,000,000
3-4 years	4,400						4,400
Over 4 years	10,034,515						10,034,515
Total	(5,980,572)	(1,534,908)	0	0	(1,063,473)	(326,317)	(8,905,270)

49. Exposure towards changes in the CPI

a. Definition

Exposure towards changes in CPI is the risk that fluctuations in the Icelandic Consumer Price Index (CPI) will affect the balance and cash flow of indexed financial instruments.

The Bank is exposed to Icelandic inflation since CPI indexed assets exceed CPI indexed liabilities. All indexed assets and liabilities are valued according to the CPI measure at any given time and changes in CPI are recognised in the income statement as interest.

b. Management

The Bank controls its indexation risk through derivatives contracts and sales and purchases of indexed bonds, mostly government bonds, and thus keeps its inflationary position within the limits set by the ALCO committee.

c. Balance of CPI linked assets and liabilities

The net balance of CPI linked assets and liabilities is specified as follows:

Net inflation exposure	30.9.2012	31.12.2011
Assets	9,148,202	6,249,421
Liabilities	(7,372,485)	(7,061,369)
Total	1,775,717	(811,948)

MP Bank hf. Amounts are in ISK thousands

Notes

50. Market risk

a. Definition
Market risk constitutes risk due to changes in interest rates and market prices of financial instruments.

b. Management
The Bank has a strict policy on controlling market risk and to keep the exposure within set limits. The risk management unit monitors market risk limits on a daily basis and reports regularly to the ALCO committee and to the CEO.

c. Market price risk
Market price risk arises from changes in the market values of securities in the Bank's portfolio, the size of which varies greatly. The Bank invests primarily in securities listed on regulated markets, but has also invested in unlisted equities and bonds. The Bank's risk is the general risk involved in investing in securities. Efforts are made to reduce this risk through active risk management.

d. Interest rate risk
The breakdown of interest rate risk associated with proprietary posision by duration is specified as follows:

Financial assets 30.9.2012	**Less than 1 year**	**1-3 years**	**3-5 years**	**5-7 years**	**More than 7 years**	**Total**
Fixed income securities in ISK	74,121	1,183,848	775,218	2,341,076	1,171,115	5,545,378
Fixed income securities in foreign currencies	108,978					108,978
Total	183,099	1,183,848	775,218	2,341,076	1,171,115	5,654,356

Financial liabilities 30.9.2012	**Less than 1 year**	**1-3 years**	**3-5 years**	**5-7 years**	**More than 7 years**	**Total**
Fixed income securities in ISK	3,683,093	242,714		269,925	742,868	4,938,600
Total	3,683,093	242,714	0	269,925	742,868	4,938,600

Net imbalance 30.9.2012	**Less than 1 year**	**1-3 years**	**3-5 years**	**5-7 years**	**More than 7 years**	**Total**
Fixed income securities in ISK	(3,608,973)	941,134	775,218	2,071,152	428,247	606,779
Fixed income securities in foreign currencies	108,978					108,978
Total	(3,499,994)	941,134	775,218	2,071,152	428,247	715,757

Financial assets 31.12.2011	**Less than 1 year**	**1-3 years**	**3-5 years**	**5-7 years**	**More than 7 years**	**Total**
Fixed income securities in ISK	274,325	593,554	513,114	12,189,920	749,184	14,320,097
Fixed income securities in foreign currencies	102,861					102,861
Total	377,185	593,554	513,114	12,189,920	749,184	14,422,958

Financial liabilities 31.12.2011	**Less than 1 year**	**1-3 years**	**3-5 years**	**5-7 years**	**More than 7 years**	**Total**
Fixed income securities in ISK	4,076,847	1,090,510	33,757	280,119	437,246	5,918,479
Fixed income securities in foreign currencies						0
Total	4,076,847	1,090,510	33,757	280,119	437,246	5,918,479

Net imbalance 31.12.2011	**Less than 1 year**	**1-3 years**	**3-5 years**	**5-7 years**	**More than 7 years**	**Total**
Fixed income securities in ISK	(3,802,522)	(496,956)	479,357	11,909,802	311,938	8,401,618
Fixed income securities in foreign currencies	102,861					102,861
Total	(3,699,662)	(496,956)	479,357	11,909,802	311,938	8,504,479

51. Operational risk

a. Definition
The risk involved in the Bank's operations is primarily linked to the risks inherent in each type of security in which the Bank invests, although there are several other factors which can also affect its operations and performance, such as incorrect analysis of investment options, employee negligence, violations of rules, problems with information systems and loss of key personnel. The Bank's reputation may be damaged, either for the above reasons or as a result of other factors which are difficult to control.

b. Management
Operational risk can be reduced through staff training, process re-design and enhancement of the control environment. The risk management and credit control unit monitors operational risk by tracking loss events, quality deficiencies, potential risk indicators and other early-warning signals. The unit takes an active role in internal control and quality management.

MP Bank hf. Amounts are in ISK thousands

Notes

Financial assets and liabilities

52. Accounting classification of financial assets and liabilities

The accounting classification of financial assets and liabilities is specified as follows:

Financial assets 30.9.2012	Held for trading	Designated at fair value	Available for sale	Held to maturity	Loans and receivables	Other at amortized cost	Total carrying amount
Cash and cash equivalents					29,583,967		29,583,967
Receivables from Central Bank					8,309,760		8,309,760
Fixed income securities	3,250,347	200,864	2,154,831				5,606,042
Shares and other variable income securities	837,930	242,531					1,080,460
Securities used for hedging		1,728,625					1,728,625
Loans to customers					23,611,085		23,611,085
Derivatives	233,806						233,806
Other assets					511,698		511,698
Total	4,322,083	2,172,019	2,154,831	0	62,016,510	0	70,665,444

Financial liabilities 30.9.2012	Held for trading	Designated at fair value	Available for sale	Held to maturity	Loans and receivables	Other at amortized cost	Total carrying amount
Deposits						44,369,409	44,369,409
Borrowings						9,165,158	9,165,158
Short positions in securities	4,864,286						4,864,286
Short positions in securities used for hedging		4,020,156					4,020,156
Derivatives	121,245						121,245
Other liabilities						5,164,119	5,164,119
Total	4,985,531	4,020,156	0	0	0	58,698,686	67,704,373

Financial assets 31.12.2011	Held for trading	Designated at fair value	Available for sale	Held to maturity	Loans and receivables	Other at amortized cost	Total carrying amount
Cash and cash equivalents					11,545,143		11,545,143
Fixed income securities	1,418,908	203,144	2,810,823	9,245,989			13,678,864
Shares and other variable income securities	844,084	224,447					1,068,531
Securities used for hedging		7,694,837					7,694,837
Loans to customers					13,294,303		13,294,303
Derivatives	199,571						199,571
Other assets					662,246		662,246
Total	2,462,563	8,122,428	2,810,823	9,245,989	25,501,692	0	48,143,496

Financial liabilities 31.12.2011	Held for trading	Designated at fair value	Available for sale	Held to maturity	Loans and receivables	Other at amortized cost	Total carrying amount
Deposits						34,594,083	34,594,083
Borrowings						2,051,155	2,051,155
Short positions in securities	4,838,963						4,838,963
Short positions in securities used for hedging		1,274,229					1,274,229
Derivatives	101,498						101,498
Other liabilities						2,147,207	2,147,207
Total	4,940,461	1,274,229	0	0	0	38,792,445	45,007,135

53. Reclassification of assets previously designated as Held to maturity

The Bank has sold certain securities that were classified as Held-to-maturity (HTM) as at 31 December 2011. Due to this tainting, the entire HTM portfolio was subsequently reclassified as Available for sale. Furthermore the Bank's use of the HTM classification is restricted in the near future.

MP Bank hf. Amounts are in ISK thousands

Notes

54. Financial assets and liabilities classified at fair value

a. 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 Bank's market assumptions. These two types of inputs result in the following fair value hierarchy:

- Level 1
  Quoted prices (unadjusted) in active markets for identical assets or liabilities. This level includes listed equity securities and debt instruments on exchanges (for example Nasdaq OMX, London Stock Exchange, Frankfurt Stock Exchange, New York Stock Exchange) and exchanges traded derivatives like futures (for example Nasdaq, S&P 500).
- 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). This level includes the majority of the OTC derivative contracts, traded loans and issued structured debt. The sources of input parameters like LIBOR yield curve or counterparty credit risk are Bloomberg and Reuters.
- Level 3
  Inputs for the asset or liability that are not based on observable market data (unobservable inputs). This level includes equity investments and debt instruments with significant unobservable components.

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

b. Use of the fair value hierarchy

The fair value of financial assets and liabilities classified at fair value is determined by the fair value hierarchy as specified:

Financial assets				**Carrying**
30.9.2012	**Level 1**	**Level 2**	**Level 3**	**amount**
Held for trading				
Fixed income securities	3,250,347			3,250,347
Shares and other variable income securities	820,122	17,807		837,930
Derivatives		233,806		233,806
Designated at fair value				
Fixed income securities			200,864	200,864
Shares and other variable income securities			242,531	242,531
Securities used for hedging	1,728,625			1,728,625
Available for sale				
Fixed income securities	2,154,831			2,154,831
Total	7,953,926	251,614	443,394	8,648,934

Financial liabilities				**Carrying**
30.9.2012	**Level 1**	**Level 2**	**Level 3**	**amount**
Held for trading				
Short positions in securities	4,864,286			4,864,286
Derivatives		121,245		121,245
Designated at fair value				
Short positions in securities used for hedging	4,020,156			4,020,156
Total	8,884,442	121,245	0	9,005,687

MP Bank hf. Amounts are in ISK thousands

Notes

Financial assets 31.12.2011	Level 1	Level 2	Level 3	Carrying amount
Held for trading				
Fixed income securities	1,418,908			1,418,908
Shares and other variable income securities	807,507	36,578		844,084
Derivatives		199,571		199,571
Designated at fair value				
Fixed income securities			203,144	203,144
Shares and other variable income securities			224,447	224,447
Securities used for hedging	7,694,837			7,694,837
Available for sale				
Fixed income securities	2,810,823			2,810,823
Total	12,732,074	236,149	427,591	13,395,815

Financial liabilities 31.12.2011	Level 1	Level 2	Level 3	Carrying amount
Held for trading				
Short positions in securities	4,838,963			4,838,963
Derivatives		101,498		101,498
Designated at fair value				
Short positions in securities used for hedging	1,274,229			1,274,229
Total	6,113,192	101,498	0	6,214,690

55. Financial assets and liabilities not classified at fair value

The fair value of financial assets and liabilities not classified at fair value is specified as follows:

Financial assets 30.9.2012	Carrying amout	Fair value	Unrealized gain
Cash and cash equivalents	29,583,967	29,583,967	0
Receivables from Central Bank	8,309,760	8,309,760	0
Loans to customers	23,611,085	23,611,085	0
Other assets	511,698	511,698	0
Total	62,016,510	62,016,510	0

Financial liabilities 30.9.2012	Carrying amout	Fair value	Unrealized gain
Deposits	44,369,409	44,369,409	0
Borrowings	9,165,158	9,165,158	0
Other liabilities	5,164,119	5,164,119	0
Total	58,698,686	58,698,686	0

Financial assets 31.12.2011	Carrying amout	Fair value	Unrealized gain
Cash and cash equivalents	11,545,143	11,545,143	0
Fixed income securities	9,245,989	9,740,512	494,523
Loans to customers	13,294,303	13,294,303	0
Other assets	662,246	662,246	0
Total	34,747,681	35,242,204	494,523

Financial liabilities 31.12.2011	Carrying amout	Fair value	Unrealized gain
Deposits	34,594,083	34,594,083	0
Borrowings	2,051,155	2,051,155	0
Other liabilities	2,147,207	2,147,207	0
Total	38,792,445	38,792,445	0

MP Bank hf. Amounts are in ISK thousands

Notes

Segment information

56. Segment analysis

a. Business segments
The Bank defines four main business segments and internal reporting to senior management and the board of directors reflects that segmentation. The segments are:

- **Asset Management**, which is divided into Asset Management and Private Banking, and serves primarily insitutional investors and high net worth individuals.
- **Investment Banking**, which is divided into Corporate Finance, Capital Markets, Credit, Proprietary Trading and Treasury, and serves institutional and private investors and corporate clients.
- **Retail Banking**, which provides selected banking services with a special focus on small and medium sized enterprises.
- **Asset Financing**, which provides equipment financing to individuals and corporate clients.

Other operations, including most subsidiaries, legacy assets and operations, form a fifth reporting segment.

b. Segment reporting
Segment performance is evaluated based on earnings before tax. Assets and liabilities are allocated to business segments and the segments pay and receive interest from Treasury to reflect the allocation of capital and funding costs. All equity is allocated to Treasury. Administrative expenses of support functions are allocated to business segments based on the underlying cost drivers.

c. Business segment results
The mechanisms for allocation of assets, liabilities, calculations of internal cost of capital and allocation of shared expenses are still under development and subject to change. This work will be completed in the second half of the year and the Bank will publish the results of individual segments in the full year financial statements for 2012.

57. Geographical information

9m 2012	**Net operating income**	**Total assets**
Iceland	2,881,371	73,915,539
Lithuania	49,338	404,089
Other regions and eliminations	57,746	(1,147,621)
Total	2,988,455	73,172,007

9m 2011*	**Net operating income**	**Total assets**
Iceland	488,150	50,589,522
Lithuania	27,462	1,627,613
Other regions and eliminations	78,152	(1,489,884)
Total	593,763	50,727,251

MP Bank hf. Amounts are in ISK thousands

Notes

Income statement

58. Net interest income

Interest income is specified as follows:

	Q3 2012	Q3 2011*	9m 2012	9m 2011*
Cash and cash equivalents	366,016	172,181	723,235	308,946
Derivatives	18,531	53,226	139,534	160,137
Loans to customers	475,019	167,380	1,168,633	256,532
Other interest (expense) income	(3,084)	68,233	486,180	90,655
Total	856,482	461,020	2,517,582	816,270

Interest expense is specified as follows:

	Q3 2012	Q3 2011*	9m 2012	9m 2011*
Deposits	307,045	274,824	1,032,194	667,630
Borrowings	85,357	2,635	148,476	914
Subordinated liabilities	0	0	0	0
Other interest expense	11,717	2,634	33,501	11,952
Total	404,119	280,093	1,214,171	680,497

Other interest income includes interest income from securities classified as Held to maturity and Available for sale as discussed in notes 15 and 52.

59. Fee and commission income

Fee and commission income is specified as follows:

	Q3 2012	Q3 2011*	9m 2012	9m 2011*
Banking	105,547	53,412	266,315	88,250
Capital Markets	89,027	68,719	327,311	120,786
Asset Management	110,769	(817)	281,394	(14,691)
Other	76,334	34,046	194,584	54,369
Total	381,678	155,360	1,069,605	248,714

60. Net financial income

Net financial income is specified as follows:

	Q3 2012	Q3 2011*	9m 2012	9m 2011*
Gain on shares and other variable income securities	22,992	11,381	13,780	34,049
Gain on fixed income securities	154,292	33,879	330,830	163,122
Dividend income	0	3	(648)	1,458
Foreign currency exchange difference	(14,614)	774	17,017	39,197
Fair value adjustments	(8,433)	0	116,853	0
Total	154,237	46,037	477,832	237,826

61. Foreign currency exchange difference

Foreign currency exchange difference is specified as follows:

	Q3 2012	Q3 2011*	9m 2012	9m 2011*
(Loss) gain on financial instruments at fair value through profit and loss	(22,933)	36,679	(31,317)	10,237
Gain (loss) on other financial instruments	8,319	(35,905)	48,334	28,960
Total	(14,614)	774	17,017	39,197
Change in the ISK trade index during the period	-0.5%	-2.6%	+1.9%	+3.2%

Note 47 provides information about the development of foreign exchange rates against the Icelandic krona.

MP Bank hf. Amounts are in ISK thousands

Notes

62. Administrative expenses

Administrative expenses are specified as follows:

	Q3 2012	Q3 2011*	9m 2012	9m 2011*
Salaries and salary related expenses	385,118	235,284	1,179,744	596,124
Other operating expenses	225,607	240,465	886,749	547,201
DIGF contributions	35,526	24,654	85,821	64,674
Depreciation and amortization	38,119	23,092	86,289	53,264
Total	684,369	523,496	2,238,603	1,261,262
Average number of full time employees during the period			115	115
Total number of full time employees at the end of the period			118	114

63. Salaries and salary related expenses

Salaries and salary related expenses are specified as follows:

	Q3 2012	Q3 2011*	9m 2012	9m 2011*
Salaries	295,342	188,735	930,266	477,917
Pension fund contributions	42,267	60,537	118,741	60,736
Financial Activity Tax	18,507	(28,426)	53,388	0
Other salary related expenses	29,002	14,437	77,350	57,471
Total	385,118	235,284	1,179,744	596,124

According to act no. 165/2003, passed in 2011, banks, and other financial institutions providing VAT exempt services, must pay a special tax levied on salary payments, a Financial Activity Tax. The current tax rate is 5.45%

64. Income tax

Profit before taxes amounts to ISK 469.7 million. Income tax amounts to ISK 32.0 million, resulting in an effective tax rate of 6.8%. This is substantially different from the Icelandic corporate tax rate of 20% due to an adjustment to the Bank's Deferred tax asset as at 31 December 2011.

65. Special tax on financial institutions

According to act no. 155/2010 on Special Tax on Financial Institutions, certain types of financial institutions, including banks, must pay annually a tax based on the carrying amount of their liabilities as determined for tax purposes. The tax rate is set at 0.041%. This tax is not a deductible expense for income tax purposes. A temporary amendment to the act passed in 2011 increases the tax rate by 0.0875% for taxes payable in 2012 and 2013.

66. Quarterly statements (unaudited)

	Q3 2011	Q4 2011	Q1 2012	Q2 2012	Q3 2012
Net interest income	180,928	322,952	377,297	473,752	452,363
Net fee and commission income	141,000	562,841	331,362	291,742	359,619
Net financial income	46,037	254,888	82,111	241,483	154,237
Share in associates	3,679	78,803	53,215	164,267	0
Other income	6,754	16,733	(25,446)	18,200	14,252
Net operating income	378,399	1,236,217	818,538	1,189,444	980,472
Administrative expenses	(523,496)	(865,729)	(732,899)	(821,334)	(684,369)
Impairment of loans and receivables	(20,983)	(64,710)	(36,501)	(217,268)	(26,376)
Pre-tax profit (loss)	(166,080)	305,779	49,137	150,842	269,728
Income tax	38,530	(61,913)	(9,096)	(29,545)	6,623
Special tax on financial institutions	(18,905)	(20,725)	(18,000)	(24,835)	(22,473)
Profit (loss)	(146,454)	223,140	22,041	96,462	253,878

MP Bank hf. Amounts are in ISK thousands

Notes

Statement of Financial Position

67. Cash and cash equivalents

Cash and cash equivalents are specified as follows:

	30.9.2012	31.12.2011
Cash	139,970	123,762
Balances with banks	4,887,858	4,661,380
Central Bank Depository Certificates	24,556,140	6,760,002
Total	29,583,967	11,545,143

68. Fixed income securities

Fixed income securities are specified as follows:

	30.9.2012	31.12.2011
Government bonds	4,264,509	13,136,745
Treasury bills	108,978	0
Listed bonds	1,031,692	338,975
Unlisted bonds	200,864	203,144
Total	5,606,042	13,678,864

69. Shares and other variable income securities

Shares and other variable income securities are specified as follows:

	30.9.2012	31.12.2011
Listed shares	148,380	86,938
Listed unit shares	175	152
Unlisted shares	159,085	175,254
Unlisted unit shares	772,821	806,188
Total	1,080,460	1,068,531

70. Securities used for hedging

Securities used for hedging are specified as follows:

	30.9.2012	31.12.2011
Government bonds	0	6,813,795
Listed bonds	200,000	153,924
Listed shares	1,528,625	727,118
Total	1,728,625	7,694,837

71. Loans to customers

Loans to customers are specified as follows:

	30.9.2012	31.12.2011
Loans to customers, gross amount	24,064,804	13,502,700
Specific allowance for impairment losses	(317,852)	(152,467)
Collective allowance for impairment losses	(135,867)	(55,929)
Total	23,611,085	13,294,303

72. Allowance for impairment losses

Change in allowance for impairment losses is specified as follows:

30.9.2012	**Specific**	**Collective**	**Total**
Balance as at 1 January 2012	187,629	55,819	243,448
Charge to the income statement during the period	200,097	80,048	280,145
Final write-offs	(41,623)	0	(41,623)
Balance as at 30 September 2012	346,103	135,867	481,970

MP Bank hf. Amounts are in ISK thousands

Notes

31.12.2011	Specific	Collective	Total
Balance as at 1 January 2011	0	0	0
Charge to the income statement during the year	188,391	55,819	244,210
Final write-offs	(752)	0	(752)
Translation difference	(9)	0	(9)
Balance as at 31 December 2011	187,629	55,819	243,448

The impairment allowance is subtracted from the following items in the statement of financial position:

	30.9.2012	31.12.2011
Loans to customers	453,718	208,397
Other assets	28,251	35,051
Total	481,970	243,448

73. Group entities

The Bank holds 11 subsidiaries, all of which are included in the Consolidated Interim Financial Statements. They are specified as follows:

	Domicile	Share 30.9.2012	Share 31.12.2011
Axia Asset Management UAB	Lithuania	100%	100%
Fasteignasjóður Íslands GP ehf.	Iceland	70%	-
Heildun UAB	Lithuania	100%	100%
Horn Florida Ltd.	UK	100%	100%
Júpíter rekstrarfélag hf.	Iceland	100%	100%
KFP ehf.	Iceland	100%	100%
LV31 ehf.	Iceland	100%	-
Lykillán ehf.	Iceland	100%	-
M-Investments ehf.	Iceland	100%	100%
M8 ehf.	Iceland	100%	-
MP Pension Funds Baltic UAB	Lithuania	100%	100%

The merger of the Bank with ALFA verðbréf hf., a subsidiary of the Bank in 2011, was completed during the period. The merger had an immaterial effect on the income statement or statement of financial position.

The Bank acquired three new direct subsidiaries and one indirect subsidiary during the period, M8 ehf., LV31 ehf., Lykillán ehf. and Fasteignasjóður Íslands GP ehf. The consideration transferred, and effect on income statement and statement of financial position, was immaterial in all cases.

The Bank has initiated a voluntary winding down of KFP ehf. The process is expected to be completed during the financial year and will have an immaterial effect on the income statement and statement of financial position.

74. Investment in associates

a. Information about associated companies at the end of the period:

30.9.2012	Domicile	Share	Share in results	Book value
GAM Management hf.	Iceland	26.8%	67,402	178,017
Londonderry Associates LLC	USA	38.0%	0	70,875
Teris	Iceland	50.2%	150,080	309,021
Total			217,482	557,913

31.12.2011	Domicile	Share	Share in results	Book value
GAM Management hf.	Iceland	36.8%	41,528	176,528
Londonderry Associates LLC	USA	38.0%	0	69,803
Teris	Iceland	28.6%	(13,809)	158,941
Total			27,719	405,272

The Bank sold a 9.99% share in GAM Management hf. during the period. The sale had an immaterial effect on the income statement and statement of financial position.

Teris has sold all material assets and operations to Reiknistofa Bankanna hf., and is in the process of winding down its operations. This process is expected to be completed in 2013.

MP Bank hf. Amounts are in ISK thousands

Notes

b. Changes in investments in associates are specified as follows:

	30.9.2012	31.12.2011
Balance at the beginning of the year	405,272	170,955
Acquisition of shares in associates	534	201,683
Disposal of shares in associates	(65,913)	0
Reclassification	0	(38,409)
Share in results of associates	217,482	66,128
Translation difference	537	4,915
Total	557,913	405,272

75. Intangible assets

Intangible assets are specified as follows:

30.9.2012	**Software**	**Goodwill**	**Other**	**Total**
Balance as at 1 January 2012	181,588	599,930	342,339	1,123,857
Additions	29,782	0	0	29,782
Amortization	(25,121)	0	(13,811)	(38,932)
Translation difference	0	0	0	0
Balance as at 30 September 2012	186,249	599,930	328,528	1,114,707

31.12.2011	**Software**	**Goodwill**	**Other**	**Total**
Balance as at 1 January 2011	0	0	0	0
Additions	237,362	599,930	356,150	1,193,443
Impairment	(27,302)	0	0	(27,302)
Amortization	(28,592)	0	(13,811)	(42,403)
Translation difference	120	0	0	120
Balance as at 31 December 2011	181,588	599,930	342,339	1,123,857

Intangible assets with indefinite useful life, such as goodwill, are not amortized but are subject to an annual inpairment test as described in note 28. As there have been no indications of an impairment the tests will be performed in the second half of 2012 and the results disclosed in the full year financial statements for 2012.

76. Property and equipment

Property and equipment is specified as follows:

30.9.2012	**Real estate**	**Other**	**Total**
Balance as at 1 January 2012	199,553	129,047	328,599
Additions	460,400	32,659	493,059
Disposals	(17,293)	(3,015)	(20,308)
Depreciation	(15,399)	(31,958)	(47,357)
Translation difference	698	14	712
Balance as at 30 September 2012	627,958	126,747	754,706

31.12.2011	**Real estate**	**Other**	**Total**
Balance as at 1 January 2011	0	0	0
Additions	348,441	160,134	508,575
Disposals	(129,375)	(9,030)	(138,405)
Impairment	0	(408)	(408)
Depreciation	(19,833)	(21,727)	(41,559)
Translation difference	320	77	397
Balance as at 31 December 2011	199,553	129,047	328,599

Real estate is specified as follows:	**Official value**	**Insurance value**	**Book value**
Office buildings in Reykjavik, Iceland	272,205	410,800	543,971
Office buildings in Vilnius, Lithuania	-	-	83,988
Balance as at 30 September 2012			627,958

Amounts are in ISK thousands

Notes

77. Other assets

Other assets are specified as follows:

	30.9.2012	31.12.2011
Accounts receivable and prepayments	511,698	662,246
Total	511,698	662,246

78. Deposits

Deposits are specified as follows:

	30.9.2012	31.12.2011
Demand deposits	35,740,620	27,799,381
Time deposits	8,628,789	6,794,702
Total	44,369,409	34,594,083

79. Borrowings

Borrowings are specified as follows:

	30.9.2012	31.12.2011
Repo transactions and overnight borrowings from the Central Bank	1,619,747	0
Money market deposits	7,544,804	2,049,678
Other borrowings	607	1,477
Total	9,165,158	2,051,155

80. Short positions in securities

Short positions in securities are specified as follows:

	30.9.2012	31.12.2011
Government bonds	4,787,110	4,769,566
Listed bonds	76,935	68,954
Listed shares	241	443
Total	4,864,286	4,838,963

81. Short positions in securities used for hedging

Short positions in securities used for hedging are specified as follows:

	30.9.2012	31.12.2011
Government bonds	4,020,156	1,274,229
Total	4,020,156	1,274,229

82. Other liabilities

Other liabilities are specified as follows:

	30.9.2012	31.12.2011
Unsettled securities transactions	1,024,620	720,821
Accounts payable	178,175	410,745
Withholding taxes	268,555	405,635
Other liabilities	3,692,770	610,006
Total	5,164,119	2,147,207

MP Bank hf. Amounts are in ISK thousands

Notes

83. Equity

a. Share capital

	30.9.2012	31.12.2011
Share capital according to the Bank's Articles of Association	5,554,000	5,554,000
Nominal amount of treasury shares	4,000	4,000

b. Capital adequacy ratio (CAD)

Equity at the end of the period was ISK 5,399 million, equivalent to 7.4% of total assets according to the statement of financial position. The capital adequacy ratio of the Bank, calculated in accordance with Article 84 of the Act on Financial Undertakings, is 14.3%. The minimum according to the Act is 8.0%. The ratio is calculated as follows:

Tier 1 capital	**30.9.2012**	**31.12.2011**
Recorded capital	5,398,634	5,068,954
Goodwill and intangibles	(1,114,707)	(942,269)
Shares in financial institutions	(178,017)	(176,528)
Subordinated fixed income securities	(99,615)	(99,615)
Deferred tax asset	(79,237)	(107,872)
Total	3,927,057	3,742,670

Capital requirements	**30.9.2012**	**31.12.2011**
Credit risk	1,674,224	1,013,321
Market risk	250,948	270,940
Operational risk	274,497	274,497
Total	2,199,669	1,558,758

Surplus capital	1,727,388	2,183,912
Capital adequacy ratio (CAD)	14.3%	19.2%

c. Capital management

A capital plan is prepared on an annual basis and approved by the Board, with the objective of maintaining both the optimal amount of capital and the mix between the different components of capital. The Bank’s policy is to hold capital in a range of different forms and from diverse sources.

The Icelandic Financial Supervisory Authority (FME) supervises the Bank on a consolidated basis and, as such, receives information on the capital adequacy of, and sets capital requirements for, the Bank as a whole.

MP Bank hf. Amounts are in ISK thousands

Notes

Other information

84. Off-balance sheet obligations

a. Lease agreements

The Bank has entered into long-term lease agreements for the office premises in Ármúli 13a and Höfðatún 2 in Reykjavík. Monthly lease payments amount to ISK 4.6 million and the agreements expire in 2015.

85. Related parties

a. Definition of related parties

The Bank has a related party relationship with its associates as disclosed in note 74, large shareholders, board members, CEO and key employees (together referred to as management), close family members of these parties and companies where related parties are large shareholders.

b. Arm's length

All transactions with related parties are carried out at arm's length and subject to an annual review by the Bank's internal and external auditors.

c. Balances with related parties

	30.9.2012	31.12.2011
Loans to management and related companies	3,724	0
Loans to large shareholders and related companies	8,238	12,099
Loans to board members and related companies	37,408	0
Deposits from management and related companies	10,326	13,544
Deposits from large shareholders and related companies	61,448	18,434
Deposits from board members and related companies	43,652	9,879
Deposits from associates	26,865	105,099

d. Off-balance sheet obligations

As at 30 September 2012 and 31 December 2011 there were no off-balance sheet obligations with related parties.

e. Transactions with related parties

	9m 2012	9m 2011*
Interest income from loans to management and related companies	224	0
Interest income from loans to large shareholders and related companies	494	723
Interest income from loans to alternate board members and related companies	2,177	0
Interest expense on deposits from management and related companies	390	247
Interest expense on deposits from large shareholders and related companies	1,584	1,352
Interest expense on deposits from board members and related companies	358	114
Interest expense on deposits from associates	1,692	1,502
Interest income from swap contracts with management and related companies	0	3,088
Fees received from related parties	605	12,358
Fees paid to related parties	129,414	121,188

Teris, an associate of the bank, was a large provider of IT services during the period.

86. Share-based payments

The Board of Directors of the Bank has approved a remuneration policy which includes a share based incentive scheme. This share based incentive scheme was approved by the Bank's Annual General Meeting in April 2012 and the Board of Directors was authorized to increase the share capital of the Bank by up to ISK 275 million in stages to fulfill any obligations arising from this scheme.

Notes

87. Supreme Court ruling no. 600/2011 on interest rate calculations on loans linked to foreign currencies

In February 2012 the Supreme Court of Iceland passed ruling no. 600/2011 in a case involving a dispute about interest rate calculations on a loan the court had previously ruled was currency indexed and as such in violation of Icelandic law. The ruling, and other rulings in comparable cases, will have no material effect on the financial statements of the Bank.

88. Changes since last full-year financial statement

The proposed merger of the Bank with ALFA verðbréf hf., a subsidiary of the Bank in 2011, was completed during the period. The merger had an immaterial effect on the income statement and statement of financial position.

The Bank has established a new business unit providing asset financing services in the form of loans and leases. The unit operates under the brand name Lykill and opened for business on 23 March 2012.