

# **Finnvera Plc's transition to International Financial Reporting Standards (IFRS)**

In accordance with a regulation laid down in 2001 by the EU Commission European companies listed in an EU securities market must prepare their consolidated financial statements in compliance with IFRS not later than for the financial year beginning on 1 January 2005 or thereafter. The European Parliament and the Council adopted the regulation in June 2002.

The Finnish Accounting Act was amended on 31 December 2004. The amendment was due to the implementation of the transitional provision included in the EU regulation, according to which application of IFRS is obligatory for those companies which have only publicly traded debt securities, for the financial periods beginning on or after 1 January 2007.

As an issuer of debt instruments Finnvera's date of transition to IFRS was 1 January 2007 and the interim financial reports are prepared in compliance with the IFRSs as adopted by the EU.

## **Most significant effects of transition to IFRS**

Finnvera finances business of small and medium-sized enterprises (SMEs), exportation and internalisation activities and operates in its role as a realiser of the government's regional policy objectives. Loans, guarantees, venture capital investments and export credits are used as financing forms.

Finnvera prepared its FAS financial statements (FAS = Finnish Accounting Standards) in compliance with the 4<sup>th</sup> chapter of the Credit Institutions Act (1607/1993), with the Ordinance issued by the Ministry of Finance regarding financial statements and consolidated financial statements of credit institutions and investment companies (1259/2000) and the standard 3.1 Financial Statements and Annual Report issued by the Finnish Financial Supervision, even though Finnvera does not operate under the Credit Institutions Act.

The most significant changes in the transition to IFRS relate to the implementation of *IAS 39 Financial Instruments: Recognition and Measurement* and *IAS 32 Financial Instruments: Disclosure and Presentation*.

The most significant change in accounting principles is the designation of all the derivatives held for hedging purposes as well as of the underlying hedged borrowings as at fair value through profit or loss (the fair value option). However, the change has no material effect on the consolidated equity. The change increased the borrowings by EUR 4,764 thousand and decreased the carrying amount of derivative liabilities by EUR 4,729 thousand in the opening balance sheet. The balance sheet comparatives at 31 December 2006 amounted to EUR -6,268 thousand and EUR 6,313 thousand.

The determination of impairment losses on receivables, on an individual or collective basis, using the discounted estimated future cash flows is a major change. The effect of discounting on the value of receivables amounted to EUR -1,671 thousand in the opening balance sheet and EUR -4,884 thousand at 31 December 2006.

Subsidies and grants received from the Finnish state are accounted for as other financial liabilities to the extent that there is a repayment obligation. The effect of the restatement on consolidated equity in the opening balance sheet amounted EUR 11,861 thousand.

## **Other aspects relating to application of IFRS**

Finnvera does not apply *IFRS 3 Business Combinations* retrospectively to those acquisitions occurred prior to 1 January 2004.

Investments in associates under Finnvera's venture capital investment strategy are accounted for as investments at fair value through profit or loss in accordance with the recognition principle applicable to venture capital investments stated in *IAS 28 Investments in Associates*.

Investment property is accounted for using the cost model as defined under *IAS 40 Investment Property*.

In the transition to IFRS the pension plans are classified either as defined contribution plans or defined benefit plans. For the defined benefit plans the difference of the present value of the pension obligations and the fair value of any plan assets is recognised in the opening balance sheet. Finnvera applied the exemption granted under IFRS 1 and recognised the cumulative actuarial gains and losses in retained earnings in the opening balance sheet.

**CONSOLIDATED BALANCE SHEET**

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1 Jan 2006

31 Dec 2006

	Ref.	IFRS			IFRS		
		FAS	adjustments	IFRS	FAS	adjustments	IFRS
<b>ASSETS</b>							
Cash and cash equivalents		0		0	0		0
Loans and receivables from credit institutions		30 829		30 829	55 196		55 196
Loans and receivables from customers	1)	1 425 723	-1 671	1 424 052	1 415 671	-4 884	1 410 787
Loans		1 396 689	-1 671	1 395 018	1 392 846	-2 867	1 389 979
Guarantee receivables		12 636		12 636	12 645		12 645
Receivables from export credit and special guarantee operations		16 398		16 398	10 180	-2 017	8 163
Investments	2)	214 479	4 627	219 106	239 897	4 627	244 525
Debt securities		98 228		98 228	106 227		106 227
Associates		51 019	4 627	55 646	51 356	4 627	55 984
Other shares and participations		62 161		62 161	77 969		77 969
Investment property		3 070		3 070	4 345		4 345
Intangible assets	3)	11 791	1 027	12 818	10 681	749	11 430
Property and equipment	2)	12 465	-4 627	7 838	14 861	-4 627	10 234
Properties		9 519	-4 627	4 892	12 152	-4 627	7 525
Equipment		2 946		2 946	2 709		2 709
Other assets		18 631		18 631	14 441		14 441
Credit loss receivables from the state		11 380		11 380	6 593		6 593
Other		7 251		7 251	7 849		7 849
Prepayments and accrued income		13 355		13 355	11 834		11 834
Tax assets	4)	664	494	1 158	4 069	1 382	5 451
<b>TOTAL ASSETS</b>		<b>1 727 937</b>	<b>-150</b>	<b>1 727 787</b>	<b>1 766 651</b>	<b>-2 753</b>	<b>1 763 898</b>
<b>LIABILITIES</b>							
Liabilities to credit institutions		693 858		693 858	701 024		701 024
Liabilities to other institutions	5)	75 510	-6 014	69 496	63 723	-4 368	59 355
Debt securities in issue	5)	375 611	10 778	386 389	353 472	-1 900	351 572
Derivatives	5)	13 143	-4 729	8 414	19 390	6 313	25 703
Provisions	6)	2 250	1 215	3 465	2 250	1 131	3 381
Other liabilities	7)	16 106	11 861	27 967	15 741	12 698	28 439
Accruals and deferred income		72 258		72 258	94 682		94 682
Capital loans		11 500	0	11 500	11 500	0	11 500
Tax liability		232	2	234	403	1	404
<b>TOTAL LIABILITIES</b>		<b>1 260 468</b>	<b>13 113</b>	<b>1 273 582</b>	<b>1 262 185</b>	<b>13 876</b>	<b>1 276 061</b>
<b>EQUITY</b>							
Equity attributable to the parent company's shareholders		460 789		447 526	495 892		479 263
Share capital		196 605		196 605	196 605		196 605
Share premium		51 036		51 036	51 036		51 036
Legal reserve		177 334		177 334	0		0
Fair value reserve		500		500	1 052		1 052
Unrestricted funds		35 314	-13 263	22 051	247 199	-16 629	230 570
Fund for domestic operations		0		0	129 852		129 852
Fund for export credit guarantees and special guarantee operations		0		0	80 223		80 223
Other		59		59	59		59
Retained earnings		35 255	-13 263	21 992	37 065	-16 629	20 436
Minority interest		6 679		6 679	8 574		8 574
<b>TOTAL EQUITY</b>		<b>467 468</b>	<b>-13 263</b>	<b>454 205</b>	<b>504 466</b>	<b>-16 629</b>	<b>487 837</b>
<b>TOTAL LIABILITIES AND EQUITY</b>		<b>1 727 937</b>	<b>-150</b>	<b>1 727 787</b>	<b>1 766 651</b>	<b>-2 753</b>	<b>1 763 898</b>

**CONSOLIDATED INCOME STATEMENT 1 Jan - 31 Dec 2006**

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	Ref.	IFRS		
		FAS	adjustments	IFRS
Interest income		<b>84 594</b>		<b>84 594</b>
Loans		59 824		59 824
Subsidies passed on to customers		17 966		17 966
Export credit and special guarantees receivables		506		506
Guarantee receivables		1 856		1 856
Other		4 441		4 441
Interest expenses	1)	<b>-34 527</b>	<b>-30</b>	<b>-34 557</b>
Other interest subsidies		<b>1 069</b>		<b>1 069</b>
<b>NET INTEREST INCOME</b>		<b>51 136</b>	<b>-30</b>	<b>51 106</b>
Net fee and commission income		<b>58 570</b>		<b>58 570</b>
Gains and losses from financial instruments carried at fair value	5)	<b>-1 659</b>	<b>-10</b>	<b>-1 669</b>
Net income from investments		<b>5 387</b>		<b>5 387</b>
Shares and participations		2 951		2 951
Investment property		-189		-189
Associates		2 625		2 625
Other operating income		<b>8 254</b>		<b>8 254</b>
Administrative expenses		<b>-42 252</b>	<b>108</b>	<b>-42 144</b>
Employee benefit expenses		-28 701	108	-28 593
Wages and salaries	3)	-22 464	19	-22 445
Social security costs	3) ja 6)	-6 237	89	-6 148
Other administrative expenses		-13 551		-13 551
Other operating expenses	3)	<b>-8 968</b>	<b>-303</b>	<b>-9 270</b>
Net impairment loss on financial assets	1)	<b>-25 017</b>	<b>-3 183</b>	<b>-28 199</b>
Loans and guarantees		-35 159	-1 196	-36 355
Credit loss compensation from state		14 986		14 986
Export credit and special guarantee		-4 843	-1 987	-6 830
<b>PROFIT BEFORE INCOME TAX</b>		<b>45 451</b>	<b>-3 417</b>	<b>42 034</b>
Income tax expense		<b>-10 976</b>	<b>888</b>	<b>-10 088</b>
Current tax expense		-10 976		-10 976
Deferred tax expense	4)		888	888
<b>PROFIT FOR THE PERIOD</b>		<b>34 475</b>	<b>-2 529</b>	<b>31 946</b>
Attributable to				
Equity holders of the parent company		34 551		32 023
Minority interest		-77		-77

**RETAINED EARNINGS**

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**1 Jan 2006**

**31 Dec 2006**

Retained earnings under FAS	35 255	37 065
IAS 12 Income Taxes	493	1 383
IAS 19 Employee Benefits	-1 215	-1 131
IAS 20 Accounting for Government Grants and Disclosure of Government Assistance	-11 861	-12 698
IAS 38 Intangible Assets	1 027	749
IAS 39 Financial Instruments: Recognition and Measurement	-1 707	-4 931
<b>Retained earnings under IFRS</b>	<b>21 992</b>	<b>20 436</b>

## **Notes to the reconciliations of equity at 1 January 2006 and 31 December 2006 and profit for the period of 1 January - 31 December 2006**

### ***1) Loans and receivables***

Under IFRS an impairment loss on loans and loan portfolios measured at amortised cost is determined as a difference between the asset's carrying amount and the estimated future cash flows discounted at the original effective interest rate.

If a financial asset has been written down as a result of an impairment loss, interest income is thereafter accrued on the impaired balance amount using the original effective interest rate of that asset.

Under FAS impairment losses were determined individually and collectively without discounting.

In the transition to IFRS the effect of the implementation of discounting method on recognition of impairment losses in the balance sheets amounted to EUR -1,671 thousand at 1 January 2006 and EUR -4,884 thousand at 31 December 2006. The impact on profit for the period of 1 January - 31 December 2006 totaled EUR -3,213 thousand, of which loans accounted for EUR -1,196 thousand and recovery receivables related to export guarantees as a whole EUR -2,017 thousand.

### ***2) Investments / Property and equipment***

Investment property is reclassified from Property and equipment into Investment securities if the Group ownership is or exceeds 20 %.

### ***3) Intangible assets***

Costs relating to development of computer software that were expensed in accordance with the previous GAAP are capitalised as certain capitalisation criteria set under *IAS 38 Intangible Assets* are met. Capitalisation increased the opening balance sheet total by EUR 1,027 thousand and the closing balance sheet total at 31 December 2006 by EUR 749 thousand. The amortisation for the period amounted EUR 303 thousand.

### ***4) Tax assets***

As a result from the transition, the effect of deferred tax assets on the opening balance sheet amounted EUR 494 thousand and on the balance sheet at 31 December 2006 EUR 1,382 thousand. Increase in deferred tax assets is due to the implementation of the discounting method in recognition of impairment losses and in fair value measurement of borrowings and related derivatives held for hedging purposes. The impact on profit for the period of 1 January - 31 December 2006 amounted to EUR 888 thousand.

### ***5) Liabilities to other institutions, debt securities in issue and derivatives***

Borrowings are mainly hedged against interest rate risk and exchange rate risk. Interest rate swaps as well as interest and currency swaps are used as hedging instruments.

Under FAS derivatives were measured at cost as permitted in the Credit Institutions Act since the liabilities to be hedged were also measured at cost except for exchange rate differences caused by changes in exchange rates.

In the transition these liabilities and related hedging derivatives are designated as "financial instruments at fair value through profit or loss" and the fair value option is applied to liabilities. These items are measured at fair value and the resulting fair value change is recognised in the income statement.

Effect of the change in classification was:

	1 Jan 2006	31 Dec 2006
Liabilities to other institutions	-6,014 teur	-4,368 teur
Debt securities in issue	10,778 teur	-1,900 teur
Derivatives	-4,729 teur	6,313 teur
<i>Total</i>	<i>-35 teur</i>	<i>-45 teur</i>

#### **6) Provisions**

A provision of EUR 1,215 thousand for the defined benefit pension plans was recognised in the opening balance sheet and at 31 December 2006 this provision amounted EUR 1,131 thousand. The effect on the income statement, EUR 84 thousand, decreased the employee benefit expense of the period of 1 January - 31 December 2006.

#### **7) Other liabilities**

The subsidies and grants received from the Finnish state, amounting to EUR 11,861 thousand, are reclassified to be presented as other liabilities in the opening balance sheet. As these grants received for the purpose of establishing a subsidiary in certain situations involve a repayment obligation they are considered a liability in nature in accordance with IAS 32 *Financial Instruments: Disclosure and Presentation*. The consolidated retained earnings are restated respectively.

## **Most significant changes in accounting principles**

### **Financial instruments**

#### ***Classification***

Financial assets and liabilities are classified as financial assets at fair value through profit or loss, loans and receivables, available-for-sale financial assets, financial liabilities at fair value through profit or loss and other financial liabilities.

#### ***Financial instruments at fair value through profit or loss***

Financial items at fair value through profit or loss comprise derivatives and those liabilities designated at fair value through profit or loss for which interest rate risk or currency risk has been hedged with these derivatives.

Based on its risk management strategy Finnvera treats these instruments applying the fair value option in accordance with IAS 39 *Financial Instruments: Recognition and Measurement*.

Finnvera does not have derivatives held for trading.

Fair value changes in assets at fair value through profit or loss are recognised in income statement in the item "Gains and losses from financial instruments carried at fair value".

Venture capital investments made by the Group are classified as financial assets at fair value through profit or loss upon initial recognition. Such investments are measured at fair value and the resulting change in fair value is recognised in the income statement as incurred. (For the fair value of venture capital investments; see the paragraph Determination of fair value).

#### ***Loans and receivables***

Contracts with fixed or determinable payments that are not quoted in an active market are classified as loans and receivables. Upon initial recognition loans and receivables are measured at fair value plus any directly attributable costs. Subsequently these items are measured at amortised cost using the effective interest method.

An impairment loss is recognised on loans and receivables when there is objective evidence of impairment as a result of one or more loss events that have an impact on the estimated future cash flows from the receivables.

Impairment is assessed both individually and collectively based on loan portfolios. Those receivables with significant customer risk are assessed individually. For the collective impairment assessment purposes receivables are grouped based on their similar credit risk.

An impairment loss is recognised if the present value of the future cash flows, discounted using the original effective interest rate of the receivable, is less than the carrying amount of the receivable. The amount obtainable from a realisation of a collateral and credit loss compensations obtainable from the state are taken in consideration in the assessment.

#### ***Available-for-sale financial assets***

Debt securities as well as shares and participations are classified as available-for-sale financial assets. Upon initial recognition these assets are measured at fair value plus any transaction costs directly attributable to the acquisition. Subsequently available-for-sale financial assets are measured at fair value and the change in fair value is recognised directly in equity in the fair value reserve. If there is objective evidence of impairment on an asset classified as an available-for-sale financial asset the accumulated loss recognised in equity is transferred in the income statement.

### ***Other financial liabilities***

Other financial liabilities comprise those other liabilities to credit institutions and customers as well as debt securities in issue that are not classified as financial liabilities at fair value through profit or loss.

Also the state subsidies and grants received for the purpose of acquisition of subsidiaries are classified as other financial liabilities based on the repayment obligation relating to these assets in certain situations.

IAS 32 *Financial Instruments: Presentation and Disclosure* defines a financial liability as a contractual obligation to deliver financial assets to another entity and an equity instrument as any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities.

Upon initial recognition financial liabilities are recorded in the balance sheet at the amount of the consideration received, adjusted for any transaction costs incurred, and are subsequently measured at amortised cost using the effective interest method.

Finnvera treats the capital loan granted for the Group at nominal amount due to its special nature and related special clauses.

### ***Determination of fair value***

Fair value of financial instruments is determined on the basis of published price quotations in an active market. If a published price quotation in an active market does not exist for a financial instrument in its entirety, but active markets exist for its component parts, fair value is determined on the basis of relevant market prices for the component parts. If the market is not active or the security is unlisted, fair value is established by using generally accepted valuation techniques.

Fair values of venture capital investments are determined using an applicable valuation method and in accordance with the guidelines of European Venture Capital Association (EVCA). The effect of any options and conversion options on the value of the ownership is taken into consideration when determining fair value. If a reliable determination of fair value is not possible, venture capital investments are measured at cost less any impairment losses.

### ***Recognition and derecognition of financial assets and liabilities***

Loans and receivables are recognised in the balance sheet when a customer takes out a loan, available-for-sale financial assets and derivatives using trade date accounting and financial liabilities at fair value through profit or loss when the consideration is received.

Financial assets are derecognised from the balance sheet when the contractual right to the asset expires or when the rights are transferred to another party. Financial liabilities are derecognised when the related obligations are fulfilled.

### ***Revenue***

Interest income and interest expenses are recognised in the income statement over the maturity of the contract using the effective interest rate method. All fees received and paid, interest points that are an integral part of the effective interest rate of the contract, as well as transaction costs and any other premiums or discounts are taken into consideration in calculating the effective interest. Interest and provision subsidies received from the state are recognised correspondingly over the maturity of the contract using the effective interest rate method.

Credit and guarantee fees are recognised in the income statement over the maturity of the contract. Other fee income and expenses are usually recognised when the service is rendered.

Gains and losses (both realised and unrealised) from derivatives, liabilities measured at fair value and venture capital investments as well as exchange rate differences are presented under the income statement item "Gains and losses from financial instruments carried at fair value".

### ***Impairment losses on receivables and credit and guarantee losses***

An impairment loss is recorded on loans and receivables when there is objective evidence of impairment. Objective evidence of a customer's capability to fulfill obligations is based on risk classification of the customers, past experience and estimates made by management about the effect of delayed payments on accruing of receivables.

Any income from realisation of guarantees and any compensation received from the state for credit losses are taken into consideration as deductions in determining an impairment loss.

### ***Intangible assets***

Development costs of IT applications and software are capitalised at cost if their cost can be measured reliably and the asset will generate probable future economic benefits for the Group.

Costs incurred from development are amortised on a straight-line basis over their estimated useful lives (five years).

### ***Provisions***

Pension plans are classified as either defined benefit plans or defined contribution plans. Under a defined contribution plan, the Group pays fixed contributions into a pension insurance company and has no legal or constructive obligation to pay further contributions. Obligations resulting from a defined contribution plan are expensed in the period to which they relate. The cost of providing defined benefit plans is charged to the income statement over the working lives of the employees participating in the plan on the basis of actuarial calculations. The pension plan assets measured at fair value at the balance sheet date are deducted from the present value of the pension obligation to be recognised in the balance sheet.

Actuarial gains and losses are recognised in the income statement over the expected average remaining working lives of the employees participating in the plan to the extent that such gains and losses exceed the greater of 10 % of the present value of the defined benefit obligation and 10 % the fair value of any plan assets.

A provision for guarantee losses is recognised when the Group has a present legal or constructive obligation to pay a guarantee compensation, realisation of the obligation is probable and it can be estimated reliably.

### ***Income taxes***

Income taxes in the consolidated income statement consist of current tax based on the taxable profit for the period and deferred tax. Tax expense is recognised in the income statement except for deferred tax relating to items charged or credited directly to equity when that tax is itself charged or credited directly to equity.

Deferred taxes are calculated for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Tax rates enacted by the balance sheet date are used in determining deferred taxes.