



AUDIT COMMITTEE

Annual Report to the Board of Governors

For the 2011 financial year

AUDIT COMMITTEE**ANNUAL REPORT TO THE BOARD OF GOVERNORS****For the 2011 financial year****Table of Contents**

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1. INTRODUCTION

The Audit Committee is established under EIB Statute as a committee independent from the Board of Directors, both Members and Observers are appointed directly by the Board of Governors. The Audit Committee is responsible for the auditing of EIB's financial statements and verifies that the activities of the Bank conform to best banking practice.

The Audit Committee held meetings over eleven days in 2011.

This report is addressed to the Board of Governors, in accordance with the Statute and Rules of Procedure, and provides details on the work of the Audit Committee in relation to the audit of the 2011 financial statements, as well as on other activities performed since the date of the previous Annual Report.

In relation to our responsibility for auditing the EIB's accounts, we have issued the Audit Committee's Annual Statements referring to the following financial statements for the financial year 2011:

- Bank statutory;
- EIB Group consolidated under the general principles of the EU Directives;
- EIB Group consolidated according to IFRS;
- Investment Facility;
- FEMIP Trust Fund;
- EU Africa Infrastructure Trust Fund; and
- Neighbourhood Investment Facility (NIF) Trust Fund.

In the statements the Audit Committee confirms, that to the best of its knowledge and belief the financial statements prepared for the entities listed above gives a true and fair view of their financial position, of the results of their operations and cash flows for the year under review.

Besides financial reporting and audit matters we focused our attention on the progress made by the EIB in complying with best banking practice and on the risk management activities of the Bank. The following sections of this report provide further detail in this respect.

2. AUDITING ACTIVITIES

2.1 Review of Audit Work

In its work, the Audit Committee relies on the external and internal auditors, from which it receives assurance on the accuracy of financial reporting and confirmation of the effectiveness of the internal control processes. In addition, the Audit Committee obtains a representation letter from the President of the Bank, which is itself based on internal support letters from the Bank's services, confirming management's responsibility for establishing and maintaining an efficient internal control structure and its responsibility for the preparation and fair presentation of the financial statements.

2.1.1. External auditors

The day-to-day audit work is delegated to the external audit firm, KPMG, designated by the Audit Committee and reporting directly to us.

In the context of the 2011 audit planning 3 priority audit areas were identified:

- lending, including valuation of the loan portfolio due to increase in credit risk (confirmed by the Bank's internal credit risk indicators) and the audit of the migration of loan contracts transferred to a new IT application as at the year end,
- treasury, including valuation of the sovereign bond portfolio and subsequent disclosures in the financial statements,
- the controls surrounding the financial reporting process, where specialist input was used for the financial statements, where due attention was given to ensure sovereign debt disclosures are in line with best practices and prevailing accounting standards.

We were briefed at length, throughout the year, on the progress and outcome of the audit procedures, in particular in relation to the priority audit areas and notably with regards to the valuation of sovereign debt and the additional sovereign debt disclosures included within the 2011 financial statements. Our regular meetings with the external auditor mean that we keep ourselves permanently briefed on the audit progress and the audit and accounting issues, resulting in a no surprises audit.

We conducted a private interview with KPMG before giving our clearance on the various financial statements. We received assurances that the audit process went as planned, with full support from the Bank services. The Audit Committee was satisfied with the results of the external audit work, which enable it to formulate its own conclusions to the Board of Governors.

The Audit Committee is also responsible for ensuring the external auditors' independence. In 2011 the Audit Committee reconfirmed with the Bank their general policy of not allowing the incumbent external auditor to undertake work outside the scope of the Framework agreement for audit services. Consequently KPMG were not engaged to perform any non audit services for the Bank during the year ended December 31, 2011.

2.1.2. Inspectorate General

The internal oversight function at the Bank is headed by the Inspector General (IG) and comprises four lines of service: internal audit (IA), fraud investigation, operations evaluations and complaints mechanism. Although the direct reporting line is to the President of the Bank, the Audit Committee has a privileged relation with the Inspector General and the Head of Internal Audit who may request private sessions with the Audit Committee and have unrestricted access to it. The Audit Committee has met regularly with IG to examine IA reports and has received updates of the status of implementation of agreed action plans (AAPs) and discussed with the Fraud Investigations Division the ongoing cases under their remit.

We have paid particular attention to the status of implementation of overdue agreed action plans, especially those considered to be of a high or medium risk, having considered the timely closure of such action plans to be of priority for the Bank, a request endorsed by the President. We have been pleased to note that no overdue high priority AAPs remain open at the year end.

In last year's Annual Report we highlighted our intention to closely monitor progress made in respect of the implementation of IA's recommendations concerning the internal procurement process. In 2012 IA completed a follow up audit of internal procurement, we took note of the successful implementation of revised procedures as a result of IA's recommendations, which have served to enhance the underlying control environment.

With reference to the IA reports discussed at Audit Committee meetings during the year we have stressed that the recommendations made by IA in respect of the derivative valuation process, concerning enhanced segregation of duties, formalised updates to existing procedures and a strengthening of the related control environment, be addressed as a matter of priority. The Bank has committed to implementing agreed actions without delay and will keep the Audit Committee briefed on progress made at the end of the 2nd quarter of 2012.

Finally the Audit Committee has received full support from the internal audit division in relation to the verification of best banking practice implementation (see section 4 below). We have been pleased to note that an internal audit review addressing the integration of best banking practice in the field of Risk Management will be performed in the coming year.

2.1.3. European Court of Auditors

The Audit Committee had its annual meeting with the European Court of Auditors, a useful occasion for exchanging information on the progress of various audits undertaken by the Court. Discussions covered subjects of common interest such as the status of current as well as future ongoing Court audits and the ongoing cooperation between the external auditors and the Court.

In October 2011 the Tripartite Agreement governing the relationship between the Bank, the European Court of Auditors and the European Commission was renewed for a period of four years.

2.1.4. Cooperation with the Audit Board of the European Investment Fund

The Audit Committee meets at least once per year with the Audit Board of the European Investment Fund in order that the two respective bodies may discuss specific areas of audit focus and share matters of interest including where possible, common working practices.

2.2 The Financial Statements as at 31 December 2011

The Audit Committee has examined the three sets of accounts issued by the EIB and those of the Investment Facility, the EU-Africa Infrastructure Trust Fund, FEMIP and the NIF Trust Fund for 2011.

The key elements of the various financial statements are presented below.

2.2.1. EIB

Statutory financial statements (non-consolidated):

The Audit Committee noted that the total balance sheet as at December 31, 2011 amounts to EUR 472 billion, an increase of EUR 52 billion, +12%, compared to the previous year (December 31, 2010: EUR 420 billion). Total own funds at December 31, 2011 have increased by EUR 2.3 billion to EUR 42.5 billion, +6%, from EUR 40.2 billion at December 31, 2010.

The evolution of the balance sheet can be explained by a year on year increase in the volume of loans to customers of EUR 23 billion to EUR 250 billion (2010: EUR 227 billion) and in the loans to credit institutions financed by a corresponding increase in debts evidenced by certificates on the liabilities side of EUR 42 billion to EUR 376 billion (2010: EUR 334 billion).

The net profit for the financial year stands at EUR 2,292 million, an increase of EUR 175 million, +8%, compared with 2010 (2010: 2,117 million).

Consolidated financial statements prepared in accordance with EU Accounting Directives.

The consolidated financial statements prepared in accordance with EU Accounting Directives comprise those of the Bank and those of its subsidiary, the European Investment Fund, the financial statements of the Fund are prepared for the same reporting year as the Bank, using consistent accounting policies.

The total balance sheet of the consolidated financial statements prepared in accordance with EU accounting directives amounts to EUR 472.5 billion at December 31, 2011 (2010: EUR 420 billion).

We note total consolidated net profit of EUR 2,268 million, slightly lower by EUR 24 million than the net profit of the unconsolidated financial statements which amounts to EUR 2,292 million, the difference is explained by consolidation adjustments and EIF's result for the year.

Consolidated financial statements prepared in accordance with IFRS.

The consolidated financial statements prepared in accordance with IFRS comprise those of the Bank and those of its subsidiary, the European Investment Fund, the financial statements of the Fund are prepared for the same reporting year as the Bank, using consistent accounting policies.

The consolidated result for the year for the financial statements prepared in accordance with IFRS stands at EUR 3,743 million, the total adjustment required to translate the financial result from the consolidated financial statements prepared in accordance with EU Accounting Directives to IFRS amounting to EUR 1,457 million. At the end of 2010 the IFRS financial result for the year amounted to EUR 2,645 million.

The variation of the financial result between EU Accounting Directives and IFRS, as well as the IFRS result year on year, is mainly explained by the variation of the fair value option accounted for in relation to loans, borrowings and ALM swaps in accordance with the requirements of IAS 39 'Financial Instruments Recognition and Measurement.' In this respect the application of fair value accounting means that the accounting value recognised in the balance sheet evolves from one period to another inline with variations in either publicly available, or deemed fair market values, of the

instruments. As the policy of the Group is to hold financial instruments designated with the fair value option to maturity, positive or negative income statement impacts are neutralised by the end of the lifecycle of the respective financial instruments.

2.2.2. Trust Funds

FEMIP The total comprehensive loss for the year 2011 amounts to EUR 2.7 million compared to a total comprehensive loss for 2010 of EUR 1.4 million, the difference year on year can be attributed to an increase in technical assistance operations and other programmes financed of EUR 1.2 million from EUR 1.4 million in 2010 to EUR 2.6 million in 2011. An increase in interest and other similar income of EUR 0.5 million has largely served to offset an increase in operating expenses of EUR 0.7 million.

EU-Africa Infrastructure Trust Fund The total comprehensive loss for the year is EUR 17.6 million compared to a total comprehensive loss of EUR 9.6 million in 2010, mainly explained by an increase in the financing of technical assistance operations, interest rate subsidies and direct grants which amounted to expenses of EUR 17.5million compared to EUR 8.4million in 2010.

The NIF Trust Fund financed technical assistance operations for the year of EUR 5.5 million and incurred a total comprehensive loss for the year of EUR 6 million compared to EUR 2 million in 2010.

3 RISK MANAGEMENT ACTIVITIES

We draw up our work plan with the objective of obtaining a good understanding of the Bank's activities throughout the year. We then formulate questions and request specific analyses in order to assess the risk impact of various external developments such as the evolving sovereign debt crisis as well as various internal developments in the Bank, including the launch of new products and initiatives.

During the past year, as a result of the ongoing and increasing economic uncertainty we have dedicated significant time at each of our meetings to discuss, evaluate and assess with the services responsible the Bank's risk management practices, the potential impacts of external economic developments together with the corresponding risk monitoring and mitigating techniques employed.

In obtaining our assurance in relation to risk management activities we focus on specific technical points in addition to regular reviews of various monthly, quarterly and annual risk reports. In particular over the past period the Audit Committee has focussed on topics such as credit risk monitoring, impact of the sovereign debt crisis, liquidity risk management, analysis of the results of various stress testing scenarios and capital adequacy including internal rating model validation and verification.

Credit risk monitoring

The Audit Committee held discussions throughout the year with Management concerning the trends of key risk indicators such as the capital adequacy ratio, evolution of loan gradings, large exposures, concentration risk and 'watch list' loans with a view to establishing that Risk Management is actively assessing and managing risks during challenging economic times. The Audit Committee has sought further explanations and assurances concerning the monitoring and provisioning of specific operations on the 'watch list', including raising questions concerning the nature, as well as the valuation methods (haircuts) applied, to the collateral used as a credit risk mitigant.

Impact of the sovereign debt crisis

As a result of the heightening sovereign debt crisis the Audit Committee has reviewed and discussed the analysis of the Bank's exposures, both in terms of lending activities and government bonds held in the treasury portfolios, on a country by country basis, in relation to both sovereign and sub sovereign counterparties. We have been briefed by legal representatives of the Bank on the rationale supporting the preferred creditor status from which the Bank could be expected to benefit as well as the protection afforded by the Bank's Statute.

Stress testing

During the year RM has extended the scope of stress testing to cover the impact on the capital adequacy ratio as a direct result of potential adverse economic scenarios applied to the Bank's loan portfolio, the outcome thereon was presented to the Audit Committee.

We have also requested in the first quarter of 2012 that the Bank undertake internally the European Banking Authority recapitalisation exercise of late 2011.

Liquidity Risk Monitoring

During the year we have met with RM to discuss and evaluate both the scope of the revised liquidity reporting framework of the Bank and the introduction of an indicator for available liquidity used for determining the size of the Bank's liquidity buffer. We have discussed and reviewed with RM the results of a sample of liquidity reports.

We asked the Bank to further develop stress scenarios in relation to the liabilities side of the balance sheet concerning the Bank's funding sources and liquidity planning, a recommendation also made by the Banque Centrale de Luxembourg ('BCL') refer to section 4.2 below. We are pleased to note the development and application of a revised liquidity stress test framework in this respect, which was tested during 2011 and is fully effective from the beginning of 2012.

Internal rating model validation and verification exercise

We were pleased to note that recommendations reported in 2010 by IA have with regards to the need to establish further statistical analysis to support model calibration have been implemented. We have met with the persons responsible from the Bank's services and reviewed the outcome of the analysis performed. Further detail on the work performed by the Audit Committee in relation to the capital adequacy ratio is detailed in section 4.2, 'Follow up Capital Requirements', below.

4 EIB COMPLIANCE WITH BEST BANKING PRACTICE

The year ended December 31, 2011 is the second year for which the Audit Committee has carried out the exercise of verifying compliance with best banking practice, the Framework for EIB conformity with best banking practice ('the Framework') having been jointly established by the Audit Committee and the Bank's services in 2010.

4.1 Implementation and verification methodology

The Framework is based on a hierarchical set of reference documents (e.g. EU Treaty, including the Bank's Statute, EU Directives, international standards, guidance and principles issued by regulatory bodies – collectively referred to as "standards" further in this report) that are considered relevant at a certain point in time, EIB compliance is measured against the requirements of these reference documents. On the basis of proposals from the Bank's services, the Audit Committee approves updates to the Framework on an annual basis. The Framework also covers the system of implementation, updating and verification of best banking practice – details of which are provided below.

During the year the Audit Committee has met to review the annual self-assessment of compliance with the Framework established, with each of the Directorates concerned. The meetings aimed at highlighting:

- (i) The areas where full compliance had not been achieved at the last self-assessment and the progress made, for each of the applicable standards, towards full implementation;
- (ii) Developments in standard setting (new standards and reformed standards); and
- (iii) New EIB internal developments and their possible relevance to the standards (e.g. to see whether new standards become relevant to EIB as new products/initiatives are developed or whether there is a change in compliance).

The Audit Committee considers that compliance with the Framework is a natural process which should form an integral part of written procedures, the internal control environment and daily working practices of the Bank.

To complement the self assessments reported by Directorates, the Audit Committee has requested that IA includes within its annual work plan an audit of one area of the Framework each year, with the specific objective of providing assurance regarding the integration of best banking practices into the corresponding internal written procedures of the Bank's services. In addition, when planning and performing individual audit assignments, we have asked IA to incorporate and perform tests of controls linked to the reference standards, with a view to providing further assurance in the form of an opinion on compliance. In 2012 IA will undertake such a best banking practice audit of Risk Management.

4.2 Review of specific areas in 2011-2012

The Audit Committee has met and discussed at length with the Bank's services the status of implementation of best banking practice and the results of the annual verification process, focussing in particular on progress made during the year in closing remaining compliance gaps.

In the areas of Liquidity risk management, market operations, payment systems and rogue trading measures were taken to address the few remaining compliance gaps reported and we understand the remaining requirements will be addressed in the current year.

The EIB's participation in Eurosystem liquidity operations resulted in an agreement being signed between the EIB and the Banque Centrale du Luxembourg ('BCL') which established a framework for the assessment by the BCL of the liquidity situation and liquidity risk management of the EIB. The BCL recently performed a follow up review of the status of implementation of their prior year recommendations. The Audit Committee understands that these have largely been addressed with further enhancements to current stress testing practices of the Bank expected to be finalised in the course of 2012.

Capital requirements

The Bank remains broadly compliant with the qualitative elements of the prevailing Capital Requirement Directive ('CRD'). We have noted marked progress with the matters highlighted in last year's Annual Report, in particular with reference to internal ratings coverage. The Bank has delivered on its commitment to allocate necessary resources and has met interim targets set for end of 2011 with a view to ensuring full ratings coverage by the end of 2012 as envisaged. IA recommendations endorsed by the Audit Committee concerning internal ratings models have been largely implemented with detailed work performed on the maintenance of the Internal Rating Model and the establishment of an Internal Rating Methodology Maintenance Committee.

The Audit Committee believes that, following up on a matter reported in previous year's report, as a result of the investment made by the Bank's services during the year with regards to the implementation of the CRD the Bank is now in a stronger position to support the application of the advanced internal modelling approach for capital adequacy calculations across all lines of business.

During the coming year the Bank will focus on the remaining gaps which includes an improvement of the large exposures framework and the formalisation of an ICAAP document, with a view to reporting full compliance with the CRD by the end of 2012.

Human resources

The Bank complies with the principles of sound compensation. We noted that subsequent to a recommendation from the Audit Committee last year, the Bank has documented the rules and processes for implementing the remuneration strategy and has implemented controls to ensure that the mandatory two weeks minimum holiday rule is verifiably respected by staff.

Corporate governance

The Bank follows corporate governance standards established by the EU, the OECD and the Basel Committee on Banking Supervision ('BCBS').

In 2011 the Audit Committee, whilst acknowledging the increasing coordination between the EIB and EIF risk functions, recommended that in order to further enhance compliance with the Framework, the Bank should consider enhancing the oversight of risk at group level.

Anti-Money Laundering and Combating the Financing of Terrorism (AML-CFT)

In the field of AML-CFT further work is required to close remaining compliance gaps. The Audit Committee, with the endorsement of Management is confident that the Bank's services will undertake the necessary to fully address the findings reported in this respect. We will closely monitor progress made during the year 2012.

New developments in best banking practices

The application and assessment of compliance with the Framework is an iterative process. Underlying best banking practice standards evolve over time and as such the Audit Committee requires the Bank's services to proactively consider and propose the inclusion of new or revised standards within the Framework. The Bank's services have not identified and proposed significant changes to the Framework during the year, in the coming year we will continue monitoring developments in the regulatory environment with a view to ensuring that the Framework remains up to date and that, going forward, continues to reflect prevailing best banking practices.

4.3 Conclusions

The Audit Committee regards the proper implementation and verification of compliance with best banking practice an explicit requirement of the Bank's Statute, to be of paramount importance. We have, together with the Bank's services, dedicated significant time throughout the year to focus on the status of implementation of the actions necessary to close remaining compliance gaps.

We consider that, in our second year of verifying and reporting on the Bank's compliance, the process of implementation and verification of the Framework is now well established within the Bank. The Bank is largely compliant with requirements of the Framework, with the exception of certain points brought to your attention, detailed above.

We have been pleased to note the considerable effort and evident progress made by those concerned to largely deliver on their prior commitments to the Audit Committee. There remains, however, further work to be done in the coming year, in particular in relation to the full implementation of IA recommendations concerning AML-CFT and in meeting objectives set in relation to reporting full compliance with the qualitative elements of the CRD by the end of 2012. We will closely follow the progress made by the Bank's services in this respect during the coming year.

5. ISSUES OF FOCUS FOR THE AUDIT COMMITTEE LOOKING FORWARD

Conscious of the unsettled environment within which the EIB currently operates as a direct result of the sustained turmoil in the financial markets, the ongoing sovereign debt crisis and related economic uncertainty within the EU, sound and effective risk management remains to be of paramount importance. We will continue to devote significant attention to overseeing the effective management of risks including:

- Analysis of the impact of ongoing macro economic developments, in particular in relation to the sovereign debt crisis;
- Review of the outcome of various stress testing scenarios;
- Close monitoring of counterparty rating downgrades and subsequent impacts on the Bank's risk indicators;

- The evolution and valuation of certain assets, including government bonds – or equivalent – held in securities portfolios or as collateral for loans.

With regards to EIB's compliance with best banking practice, we consider that the process of the implementation and verification of the Framework is now well established, we will concentrate, as we did this year, on monitoring and reviewing the actions undertaken by the Bank's services to close the few remaining compliance gaps, in particular in the area of Anti Money Laundering-Counter Financing of Terrorism, as well as continuing to oversee the annual verification exercise.

Within the context of compliance with best banking practice, the EIB's preparations to meet requirements of the forthcoming suite of banking regulatory reforms, will figure highly on our agenda. We will meet regularly with the services concerned to monitor and review the outcome of impact assessments as well as the status of implementation plans, in order to ensure the EIB's readiness for compliance from the outset.

We are aware of the forthcoming revisions to international financial reporting standards (IFRS), and with particular regard to IFRS 9 the standard which will replace IAS 39, will liaise with the Bank's services to understand the potential implications for the financial reporting process, including any IT system or data configuration requirements, as well as to ensure the EIB's readiness for first time application of any newly issued or revised IFRS.

Finally we intend to closely follow developments with respect to proposed reforms to the audit profession in order that the impact of any future reforms on the current external audit arrangements and practices in place at the EIB may be established, responsibility for which falls directly within the remit of the Audit Committee.

6. CONCLUSIONS

Based on work undertaken and the information received (including an unqualified opinion from the external auditors on the financial statements and a representation letter from the Management of the Bank), the Audit Committee concludes that the financial statements drawn up by the Board of Directors give a true and fair view of the financial position of the Bank and of the results of its operations and cash-flows for 2011, in accordance with the applicable accounting framework.

The Audit Committee is able to extend the same conclusion to the financial statements of the, the EU-Africa Infrastructure Trust Fund , FEMIP, and the Neighbourhood Investment Facility Trust Fund as these are covered to a large extent by the EIB's own risk control systems and internal and external audit arrangements.

The Audit Committee was able to carry out its work to fulfil its statutory mandate under normal, unrestricted conditions. The Audit Committee is satisfied that the audit assurance obtained during the meetings, corroborated by the review of the documentation presented, and its own analyses sustain its conclusions. On this basis, the Audit Committee issued its annual statements as of the date of signature of the audit report by the external auditors and of the adoption by the Board of Directors.

The Audit Committee had a balanced work approach during the year in terms of focus, objectives and means utilised to obtain the necessary assurance. The Committee believes that it has retained appropriate standing within the Bank, and that it has maintained appropriate relations with management and Bank staff, while remaining independent from the Bank at all times. In 2011 the Audit Committee received the expected support from the Bank's services, thus being able properly to discharge its responsibilities.

Date, 15 May 2012

Signed by:

E. MATHAY, Chairman

J. RODRIGUES DE JESUS, Member

D. NOUY, Member

J. GALEA, Member

M. ÜÜRİKE, Member

B. JAKOBSEN, Member

J. VESALA, Observer



AUDIT COMMITTEE

Annual Report to the Board of Governors

Investment Facility

For the 2011 financial year

AUDIT COMMITTEE**ANNUAL REPORT TO THE BOARD OF GOVERNORS
ON THE INVESTMENT FACILITY****For the 2011 financial year**Table of contents:

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1. INTRODUCTION - the role of the Audit Committee

The statutory role of the EIB's Audit Committee is to verify that the Bank's operations have been conducted and its books kept in a proper manner, as defined in the Statute and Rules of Procedure. The Financial Regulation of the Cotonou Agreement provides for the audit and discharge procedures of the Investment Facility to be the same as those defined for the Bank.

The Audit Committee issues a statement each year confirming, to the best of its knowledge and belief that the financial statements prepared for the Investment Facility give a true and fair view of its financial position, the results of its operations and of its cash flows for the respective year, in accordance with the accounting framework applied by the Bank (see section 3 for more details).

The Audit Committee is established under the EIB Statute as a committee completely independent from the Board of Directors, with the Members and Observers being appointed directly by the Board of Governors. This report from the Audit Committee to the Board of Governors provides a summary of the Committee's work focused more specifically on the Investment Facility during the period since the last annual report date.

2. AUDIT COMMITTEE REVIEW

The assurance expressed by the Audit Committee is based essentially on the external audit performed by KPMG, but also on the fact that the Investment Facility (IF) shares a number of systems with the Bank, notably those involved in risk management, human resources management, treasury management and financial reporting. The Risk Report for the Investment Facility prepared by the Bank services was also shared with us. The Audit Committee obtains an understanding of the activities and risks associated with the various developments by reviewing regular management reports and by interacting regularly with the relevant Bank services involved in the IF activities.

Meetings with Management

The Audit Committee has met during the past year with the Management of the Investment Facility, who offered details about the recent developments and future orientations for the IF and the Bank's activities in the ACP region in general. The IF portfolio was discussed, including the watch list, current project trends and the outcome of the Mid-Term evaluation of EIB activities in the ACPs and OCTs.

Monitoring Aspects

Continuing to build on progress made over the last few years with regards to enhancing the due diligence process and the control environment, the Bank has re-enforced the monitoring of operations by creating a segregated function tasked with the monitoring and post signature follow up of both loan and equity investments.

A mid term evaluation of the overall performance of the Investment Facility foreseen in the Cotonou Agreement was carried out and although not specified in the Agreement the scope of the evaluation was expanded to include projects financed from the own resources of the EIB. The report issued in 2011 concludes that the EIB has thus far fulfilled its mandate under the Cotonou Agreement and makes recommendations on ways to enhance its impact and visibility. The Audit Committee will follow up on the status of implementation of recommendations with Management in the course of the year.

External auditors (KPMG)

The external auditors report to the Committee, which delegated to them the day-to-day work concerning the audit of the financial statements. In order to be able to rely on the work performed by the external auditors, the Audit Committee has properly monitored their activity, by requesting oral and written reports, by reviewing the external auditor's deliverables and making further inquiries and through a formal interview before the sign-off of the accounts.

We held discussions with the auditors throughout the year, in order to keep ourselves briefed on the audit progress and the audit and accounting issues. We conducted a private interview with KPMG before giving our clearance on the various financial statements. We received assurances that the audit process went as planned, with full support from the Bank services.

The Audit Committee assesses regularly the external auditor's independence, including the absence of any conflicts of interests.

Inspector General

The internal oversight function at the Bank is headed by the Inspector General (IG) and comprises four lines of service: internal audit, fraud investigation, operations evaluations and complaints mechanism. Although there is no direct reporting line, the Audit Committee has a privileged relation with the Inspector General and the Head of Internal Audit who may request private sessions with the Committee and have unrestricted access to it. The Audit Committee meets regularly with IG and examines IA reports and ongoing cases with the Fraud Investigations Unit.

The Audit Committee is also informed about any alleged cases of wrongdoing and ongoing investigations relating to Bank projects, including Investment Facility operations. We also discuss with Internal Audit all the significant audit recommendations and agreed action plans, together with the unit responsible for implementation. No specific audits in relation to the Investment Facility have been performed by the EIB Internal Audit during the reporting period.

European Court of Auditors

The Audit Committee has not received from the European Court of Auditors any audit reports or audit notifications related to the Investment Facility in 2011.

3. THE FINANCIAL STATEMENTS AS AT 31 DECEMBER 2011 AND THE ANNUAL STATEMENT OF THE AUDIT COMMITTEE

The Audit Committee examined the 2011 financial statements of the Investment Facility and has interviewed the external auditors, in the presence of the Bank's management and in private, in order to obtain an understanding of the audit procedures applied.

The Committee noted, in relation to the 2011 financial statements:

- **Income statement:** The Investment Facility recorded a profit of 61 million in 2011 compared to a profit of EUR 35 million in 2010. This is mainly due to a positive net result on financial operations of EUR 18 million compared to loss on financial operations of EUR 16 million in 2010 (Note 18) and a reduction in net fee and commission income from EUR 11 million in 2010 to EUR 2 million in 2011.
- **Balance Sheet:** The Balance Sheet total increased from EUR 1,555 million at December 31, 2010 to EUR 1,825 million at December 31, 2011.
- **Credit risk:** The Investment Facility had disbursed exposure totalling EUR 1,285 million at the end of 2011, increasing from EUR 1,039 million at the end of 2010.
- **Impairment:** Certain impairment adjustments on loans recorded in previous years were reversed, reducing the balance of impairments from EUR 77 million at the end of 2010 to EUR 49 million at the end of 2011

Basis of accounting: In accordance with the Investment Facility Management Agreement ('the Agreement'), the Bank prepares financial statements guided by International Public Sector Accounting Standards or International Accounting Standards as appropriate (Article 7, paragraph 3 of the Agreement). The accounting framework applied for the year end December 31, 2011 is International Financial Reporting Standards (IFRS) as endorsed by the EU. As this is the first year of application of IFRS three years of comparative figures are disclosed in the financial statements in accordance with the requirements of IFRS 1, First-Time Adoption of IFRS.

4. CONCLUSION

In meeting its responsibilities in 2011 the aim of the Audit Committee was to achieve a balanced approach in terms of focus, issues handled and means utilised to obtain the necessary assurance. The Audit Committee is of the opinion that it has been able to carry out its work to fulfil its statutory mission under normal, unrestrictive conditions. We have received full cooperation from the Investment Facility during the reporting period.

Based on the work undertaken and the information we have received (including the opinion from the external auditor on the financial statements and a representation letter from the Management of the Bank), we conclude that the 2011 financial statements of the Investment Facility have been drawn up correctly and that they give a true and fair view of the 2011 results and financial status according to the accounting principles applicable to the Investment Facility. On this basis, we signed our annual statement as of 15 March 2012, the date on which the EIB Board of Directors has approved the submission of the IF financial statements to the Board of Governors.

Date, 15 May 2012

Signed by:

E. MATHAY, Chairman

J. RODRIGUES DE JESUS, Member

D. NOUY, Member

J. GALEA, Member

M. ÜÜRKE, Member

B. JAKOBSEN, Member



AUDIT COMMITTEE

**Response of the Management Committee
To the Annual Reports of the Audit Committee**

For the 2011 financial year

**RESPONSE OF THE MANAGEMENT COMMITTEE
TO THE ANNUAL REPORTS OF THE AUDIT COMMITTEE
FOR THE YEAR 2011**

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1 CORPORATE GOVERNANCE AND INTERNAL CONTROL

The Board of Directors has the overall responsibility for maintaining a sound system of internal control that supports the achievement of Bank's policies, aims and objectives while safeguarding the funds and assets of the Bank in accordance with the responsibilities assigned to the Board of Directors within the Statute of the European Investment Bank.

The Management Committee, under the supervision of the Board of Directors, has the day-to-day responsibility for the system of internal control which is based on an ongoing process designed to identify the principal risks to the achievement of policies, aims and objectives, to evaluate the nature and extent of those risks and to manage them efficiently, effectively, and economically. In this regard, the Management Committee continues to seek measures to enhance the risk management, audit and other internal control structures of the Bank.

The Management Committee and Bank services meet with the Audit Committee during the year and the Bank endeavours to respond promptly to requests of the Audit Committee. The Bank services have maintained a collaborative approach in supporting the work of the Audit Committee and continue to foster mutually constructive, yet appropriately independent, relationships between the Management Committee, Audit Committee, the internal auditors and external auditors. The Bank commits to maintain this collaborative approach to enable the Audit Committee to execute its responsibilities in line with its statutory provision and respecting the areas of focus identified by the Audit Committee.

In addition to an annual external audit of the financial statements under the discharge rules of the Statute, a number of the Bank's activities under partnership agreements are also subject to separate external audit scrutiny. Furthermore, various audit procedures are required in connection with certain bond issues. As both a Community body and a financial institution, the Bank also cooperates with other independent control bodies such as the European Court of Auditors, European Anti-Fraud Office (OLAF) and the European Ombudsman. As such, the Bank is subject to significant independent review throughout the year, as well as at the year end.

The Bank has a balanced approach to 'risk taking' and adopts an active approach to the mitigation of risk. The Management Committee remains satisfied that the major risks to which the Bank is exposed, as identified through the risk management and internal control framework, have been reviewed and systems, policies and/or procedures have been established to manage those risks. Overall internal controls and procedures are effectively designed and operated to provide proper assurance on the integrity, legality and timeliness of the underlying transactions and processes of the annual financial statements. Further comments on governance are given in the context of the Best Banking Practices framework in Section 3 below.

2 RISK MANAGEMENT

2.1 General Risk Management Approach

As a matter of priority, the Bank continues to review and improve its risk management framework on an on-going basis.

Looking ahead, the Bank's risk taking needs to be exercised in an even more stringent manner, in order to maintain its AAA rating and status as prime issuer on the capital markets. This entails special attention to the evolution of the credit quality of the risk portfolio and a reduction of the leverage ratio in 2012, with further reductions in 2013-2014 to return to levels preceding the beginning of the crisis – all of which have been anticipated in the Bank's Operational Plan for 2012-2014.

2.2 Specific Risk Management Activities

Credit risk monitoring

The continuous assessment of credit risk is undertaken through close monitoring of key indicators including Basel II capital adequacy ratios, review of asset quality distribution for existing portfolio and new business, managing the evolution of the Watch List, risk concentration measures and activity impact on the leverage ratio.

In the Transaction Management and Restructuring (TMR) Directorate, the Bank has and shall continue to strengthen its ability to internally monitor its counterparts and respond to contractual covenants breaches and distressed situations resulting from deteriorating financial and economic conditions. To date the Bank has not suffered significant defaults or losses.

Indeed the TMR Directorate has been yet further reinforced to significantly increase monitoring and rating coverage. Approximately 97% of all counterparts having operations with loan grading at D+ and below are now subject to on-going formal monitoring. As such and in compliance with Basel II rating coverage requirements, the Bank now ensures an annual re-rating of all exposures on which calculation of capital requirements are made based on internally estimated risk parameters.

Impact of the sovereign debt crisis

The deterioration of credit ratings suffered by several of the Bank's Shareholders and, more widely, by many of the Bank's counterparts operating in countries which are most affected by the sovereign crisis creates a challenging environment in which the Bank must operate. However the EIB remains on solid financial grounds with a high quality performing loan portfolio, strong and growing net surplus, a lean cost base, EU sovereign shareholders and associated preferred creditor status; all of which are consistently reflected in the Bank's AAA credit rating.

Stress Testing

The Bank is currently responding to the Audit Committee's request to undertake and report on the results of stress tests calculated on the basis of a mark to market valuation of sovereign exposures. This mirrors the stress tests performed during the European Banking Authority recapitalisation exercise in 2011.

3 BEST BANKING PRACTICE

3.1 Implementation and verification methodology

The Bank is committed, through its Statute, to the implementation of relevant accepted best banking practices as defined within a framework established by the Audit Committee in consultation with the Bank's services in 2010 (no new best banking practices were identified for inclusion in the Bank's framework in 2011). These best practices are complementary to the legislation and rules that are directly applicable to the Bank.

The Bank continually seeks full compliance with current relevant best banking practices, as defined within the framework, and elements for further compliance have been identified and actions, reviews or investigations are underway to address them. In 2012, Internal Audit will perform a specific review of the Risk Management area of the framework and will report the findings to the Audit Committee. It should also be noted that in all audits and Internal Control Framework reviews, the Best Banking Practice framework is referenced and incorporated where appropriate in the testing.

The Bank reiterates its recognition that evolution in banking activities will require continuous review of the best banking practices and commits to the revision, if necessary, of the Bank's associated compliance measures.

3.2 Capital Requirement Directive

In accordance with the Bank's internal compliance work plan and supported by an increase in resources, nearly all of the Capital Requirements Directive compliance gaps noted by the Audit Committee at end 2010 have been closed and as foreseen, the remainder will be totally closed by the end 2012.

Indeed, the Bank will assess how to prioritise further regular Risk Management activities required for on-going Best Banking Practice compliance. These would include validation of internal ratings, validation and back testing of models, stress testing as well as documentation thereof.

3.3 Anti-Money Laundering and combating the Financing of Terrorism

As with all forms of fraud and corruption, the Bank maintains a zero tolerance policy towards money laundering and the financing of terrorism. Improvements will continue to be made to the Bank's operations and controls based on the recommendations of a Bank commissioned internal audit in this area. In order to ensure that specific Anti-Money Laundering / Combating the Financing of Terrorism training requirements are met in 2012, the provision of training will be outsourced to a third party. A new IT filtering system which will further enhance the automatic detection of EIB counterparts and cashflows with entities listed in relevant watchlists is also being implemented.

4 THE INVESTMENT FACILITY

The Bank is entrusted with the management of the Investment Facility (IF), financed by the EU Member States' budgets. Resources from the IF, alongside the Bank's own resources (OR), are utilised in the finance of operations in the African Caribbean and Pacific Countries (ACPs) and in the Overseas Countries and Territories (OCTs). The operations flowing from the IF and the Bank's own resources are complementary in nature. IF operations typically focus on the riskier market segment of private sector projects that would normally not meet the prudential requirements set under the financing of OR supported operations.

4.1 Common platform for Management and Internal Controls

The key transactions and internal activities related to the management of the IF are handled by the same processes, procedures and infrastructure of the Bank. Hence key management and internal controls, particularly in regard to risk management, internal audit, human resources, treasury and financial reporting are the same as those applied to the operations of the EIB. External mandates, including those of the IF, are subject to external audit.

5 LOOKING AHEAD

The Bank is closely following the finalisation of the IFRS 9 components with a view to ensuring proper implementation once the standard becomes applicable in the European Union which appears to be no earlier than 2015. The new standard could offer opportunities to better control the considerable volatility currently experienced by the EIB in its IFRS consolidated results.