



Artist: Jean-Marie Biewer
Title: Paintings or Paint-Things
Material: Oil on canvas
Format: 110 x 110 cm
BCL collection

4. THE BCL AS AN ORGANISATION

4.1 Structure of the BCL

4.1.1 The Council and the Audit Committee

The Council

Article 6 of the Founding Law of 23 December 1998 defines the powers of the Council of the Bank. In 2005, the Council consisted of the following members:

- Governor: Yves Mersch
- Members: Andrée Billon
Jean Hamilius
Pit Hentgen
Mathias Hinterscheid
Serge Kolb
Patrice Pieretti
Nico Reyland
Michel Wurth

During 2005, the Council held five meetings. Within the framework of **monitoring the financial situation** of the Bank, the Council approved the financial accounts as at 31 December 2004, the budgetary trends and subsequently, the budget and the organisation chart of the Bank for the 2006 financial exercise.

The Council also observed and commented on economic and financial developments on a national and international basis and was kept informed of the decisions taken by the Governing Council of the ECB, concerning for instance the future of the national payment systems.

Within the framework of the **state budget procedure**, the BCL has given an opinion to the Financial Commission of the Chamber of Deputies. The draft opinion was previously presented to the members of the Council for their comments.

Finally, the Council appointed the members of the Audit Committee for the 2006 financial exercise.

The Audit Committee

At its meeting on 8 December 2005, the Council renewed the mandates of the non-executive members of the Audit Committee for 2006: Messrs. Pit Hentgen, Mathias Hinterscheid and Nico Reyland. Mr Mersch is an *ex officio* member in his function as Governor of the Council.

The Audit Committee held three meetings in 2005.

4.1.2 The Board of Directors

The Board of Directors is the superior executive authority of the BCL. It takes the decisions and draws up the measures necessary for the Banque centrale du Luxembourg to carry out its tasks.

Without prejudice to the independence of the Director-General with regard to all instructions in his capacity as a member of the Governing Council of the ECB, the decisions of the Board of Directors shall be taken collectively.

The Board of Directors consists of a Director-General and two Directors.

Director-General: Yves Mersch
Directors: Andrée Billon et Serge Kolb

4.1.3 Supervisory mechanisms

Various supervisory mechanisms have been set up by the BCL in order to ensure the efficient functioning of its operations in a secure environment and while respecting its budget allocations.

Internal supervisory mechanisms

The BCL's internal supervisory system is based on general rules and regulations, which are widely accepted as standards by the financial sector, and it also takes the BCL's specific needs as a central bank into consideration. The principles of internal supervision and the assignment of various responsibilities in this area are laid down in internal circulars and in the Bank's handbook of procedures.

An initial internal supervisory system concerning the general management of the BCL has been put in place by the Board of Directors. The senior management of the BCL and their staff are responsible for the proper functioning of this supervision. Some functional checks are carried out by specific administrative units, ensuring a separation of the tasks to be carried out by the BCL.

The management of financial risks is performed by the organisation and risk unit, which tracks all the portfolio positions of the BCL on a daily basis, independently of the front office. Daily reports on movements in portfolio positions that affect performance and risk exposure are sent to staff specialists and heads of unit.

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The BCL's strategic orientations are defined on the basis of performance measurement according to the Balanced Scorecard method and of the principles laid out in the *Positionnement de la Banque*, a document describing the Bank's positioning which has been approved by the Council and published on the BCL's website.

In order to obviate any risk of money laundering, a compliance officer has been supervising the BCL's banknote and coin transactions in the interest of the general public and of professionals of the financial sector since 2005.

A second level of internal supervision is provided by the internal audit unit, which analyses and evaluates on the basis of predefined objectives and a precise methodology the appropriateness and efficiency of the existing supervision. Internal audit is a supervisory unit independent of the BCL's other administrative units and it reports directly to the Governor.

The head of internal audit may also be involved in the work of the Audit Committee. Generally speaking, the internal audit unit pursues the objectives and follows the reporting procedure of the ESCB.

External supervisory mechanisms

An initial external supervision of the BCL's activities, namely the checking of its accounts, is carried out by the Bank's independent external Auditor, who is nominated yearly in a proposal sent by the Council of the Bank to the government.

At the request of the Council, the independent Auditor carries out specific complementary checks and analyses during the year. At the European level, the Auditor of the Bank is approved by the Council of Ministers upon the recommendation of the Governing Council of the ECB. In this context, the Auditor is given responsibility for particular missions with regard to the Eurosystem.

The Statute of the ESCB and of the ECB states that the central banks shall act in accordance with the guidelines and instructions of the ECB. The Governing Council of the ECB monitors respect for those provisions at the European level and may also request additional information.

4.1.4 Financial reports, annual accounts and annual budget

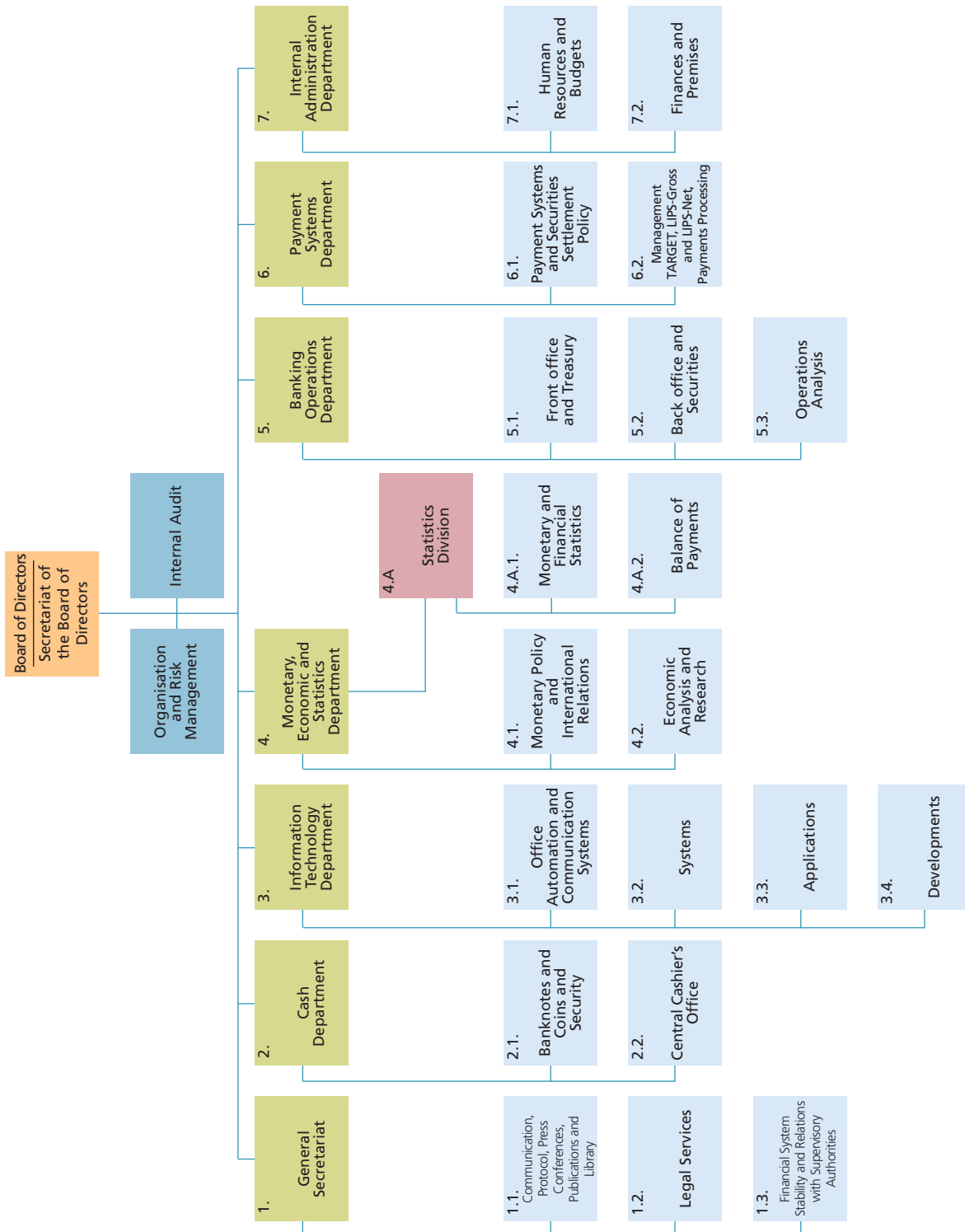
A copy of the Bank's financial reports, annual accounts and annual budget, as approved by the Council of the Bank, are presented to the government and the Chamber of Deputies. The government in Council has to decide whether to grant discharge to the BCL's decision-making bodies. This decision does not call into question the duties of the Bank within the ESCB and is taken without prejudice to the independence of the BCL vis-à-vis the government. The annual accounts and the decision granting discharge to the BCL's decision-makers are published in the *Mémorial*.

4.1.5 Corporate governance

The BCL has established a code of conduct, which defines internal and external rules of conduct applicable to all its staff. Without prejudice to public service law, social legislation or pre-existing contractual obligations, the code of conduct provides for ethical standards based on non-discrimination, solidarity, efficiency and independence which are to be strictly observed by all staff members. Moreover, certain staff members with special responsibilities are subject to particular provisions of the code of conduct.

The ECB has required, since 2002, that all members of the Governing Council observe a code of conduct which lays down the highest standards of professional ethics. The members are expected to act honestly, independently, impartially, with discretion and without regard to self-interest and to avoid any situation liable to give rise to a personal conflict of interests. They must continue to abide by these standards for one year after leaving office.

4.1.6 The BCL's organisation chart



4. THE BCL AS AN ORGANISATION

4.2 Human resources

4.2.1 Staffing

During 2005, the total number of staff slightly fell by 1.46%, reaching 203 on 31 December 2005 (including the Board of Directors), equivalent to 192.5 full-time positions and representing a 1.79% decline compared with 2004. Eight different nationalities are represented on the staff, thus contributing to the Bank's cultural diversity.

The fact that the number of staff members decreased proportionally more slowly than the number of full-time equivalent positions is the result of a constant increase in the staff members working part-time during 2005 compared with 2004.

On 31 December 2005, 21 staff members worked part-time, as follows:

- part-time work (50%): 5 staff members
- part-time work (75%): 6 staff members
- leave for part-time work: 10 staff members

An additional three staff members were on part-time parental leave.

Finally, two staff members were granted unpaid leave and two were on special leave.

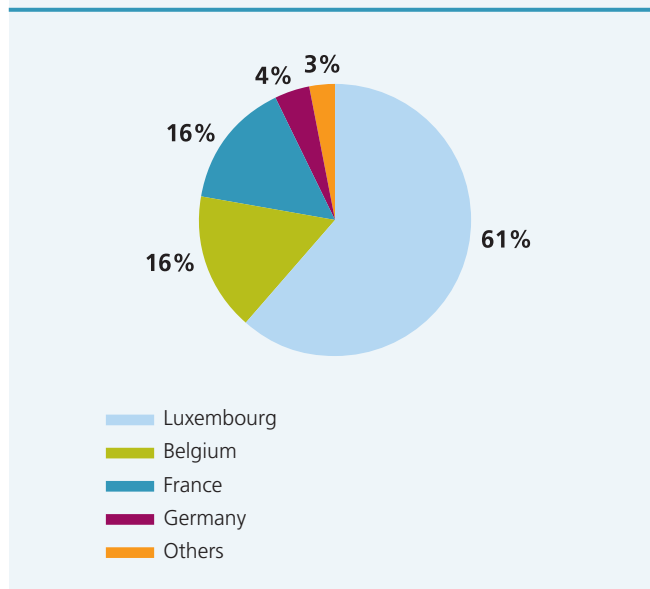
The average number of staff at the BCL in 2005 was 205.5, compared with 205 in 2004.

The overall approved headcount ceiling for 2005 amounted to 214 full-time equivalent positions. This number remains unchanged for 2006.

In 2005, four staff members left the Bank, one of whom retired. There were no recruitments. The BCL received 380 unsolicited job applications and 194 applications for internships or student jobs.

The BCL offered internships varying from six weeks to two months to eight students following university courses related to the Bank's activities and a one-year internship in the Monetary, Economics and Statistics Department to a PhD student.

CHART 1: STAFF MEMBERS BY NATIONALITY



The average age of BCL staff members slightly increased from 37.30 years in 2004 to 38.47 years as at 31 December 2005. On that date, 34% of the staff were female and 66% male.

CHART 2: STAFF MEMBERS BY AGE GROUP

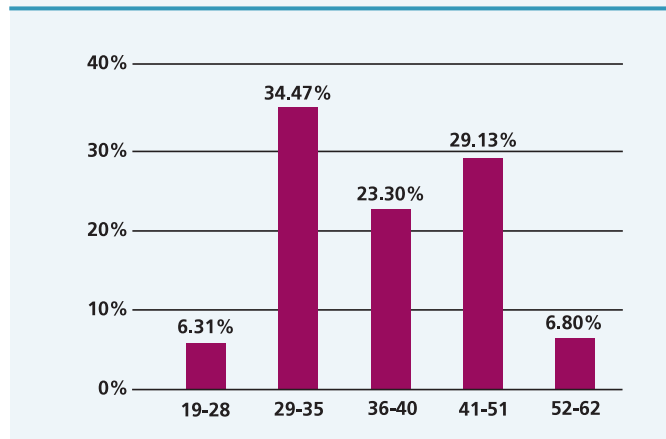
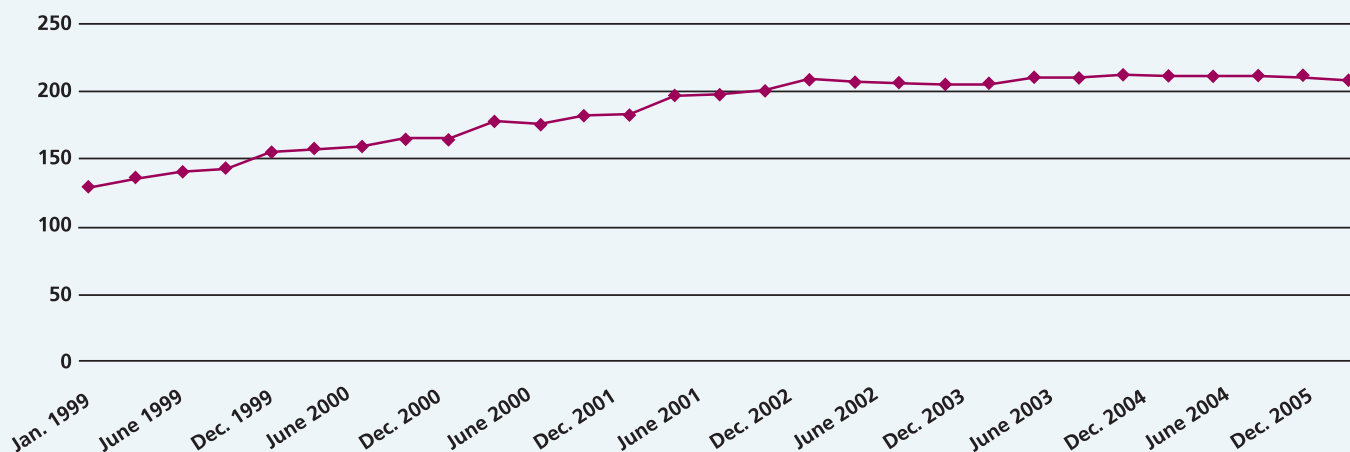


CHART 3: STAFF NUMBERS SINCE 1 JANUARY 1999



4.2.2 Human resources management

From September to November 2005, the Board of Directors commissioned an external consultant to analyse existing processes within the Bank. The study produced a diagnosis of the current situation and enabled human resources management to draw up a specific action plan to mobilise the skills of the BCL's staff members, giving them a greater say in their career development. In this context, much greater emphasis will be placed on recognising performance and on following up development possibilities (internal job rotation, working experience within the ESCB, training).

The annual appraisal of each staff member should consider how well he/she has attained specific objectives as well as identify training needs.

4.2.3 Staff training

The Bank sees itself as a centre of competence, if not excellence, and aims to keep the public's confidence. It is one of the necessary conditions for an efficient development of the Bank.

In order to make sure that training fully performs this role, a supplementary part was elaborated during 2005 in the framework of the Bank's training policy. A concept aiming at reconciling the objectives with the requirements following from the Bank's strategy with the identification of the training needs should permit the development of an efficient training plan for every staff member. Essentially, this means that defining training needs in terms of objectives should be favoured in order to make the right training choices. These needs will be identified by specialists who know the Bank's activities well and give priority to organisational effectiveness. After drawing up this very ambitious concept, it will need to be set up at the Bank in 2006 and 2007.

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The training policy to be developed within the BCL should aim:

- to develop a higher degree of professional mobility within the BCL by ensuring an appropriate balance between the staff members' skills and the Bank's requirements;
- to promote a closer identification with the Eurosystem. This goal was given clear expression in three documents adopted by the Governing Council of the ECB in January 2005: the Mission Statement, the Strategic Intents and the Organisational Principles of the Eurosystem. The training offered in this context aims to foster a team spirit and to help all staff members understand that they are an integral part of the Eurosystem.

Therefore, besides the basic internal training given to new recruits, all staff members are encouraged to do external training, mainly with other central banks in the ESCB so as to consolidate their professional skills.

4.2.4 The Pension Fund

Article 14 of the Founding Law of 23 December 1998 relating to the monetary status and the Banque centrale du Luxembourg provides that legal pension entitlements of BCL agents are determined by their status (i.e. civil servant, State employee, private employee or worker).

The costs and financing of pensions are also governed by this statute, which reads as follows (paragraph 4(b)):

"The pensions of the Bank's agents shall be paid by the Bank. These costs shall be financed by a pension fund of the Bank. The pension fund shall be financed on the one hand by statutory deductions from agents' salaries in accordance with the rules governing the pension scheme corresponding to their status, on the other hand by contributions made by the Bank itself."

The Law also provides for transitional arrangements for BCL agents who contributed previously to another pension fund, as follows: "Luxembourg pension funds which have received contributions for persons who are, or become, agents of the Bank on the day this Law enters into force, shall pay those contributions into the Bank's pension fund" and "the contribution periods of those agents to these pension funds are fully valid as contribution periods to the Bank."

The BCL's pension fund, which started operating in 2001, is governed by a set of internal rules. It has a decision-making Executive Committee (*Comité directeur*) and a consultative Tactical Benchmark Committee. The Executive Committee consists of the BCL's Board of Directors, two elected representatives from the staff, two co-opted members acting as delegated managers and one member designated by the Staff Committee.

The Luxembourg Supreme Court of Justice, in a judgement dated 20 April 2005, ordered two Luxembourg pension funds to pay to the BCL's pension fund, in accordance with Article 35 of the Founding Law of 23 December 1998, the contributions they had received.

The financial aspect having been clarified by this judgement and its subsequent enforcement, the legal aspect still requires further clarification in respect of the coordination of national, and even international, pension schemes, involving transfers to and from the BCL's pension fund.

In concrete terms, the pension fund needs to be recognised as a fully-fledged actor in the decision-making process affecting individual rights with regard to the transfer of pension rights within the country and abroad, but also in respect of the scope of decisions relating to occupational disability and the administrative coordination underlying these different fields.

The need for legal safety and the protection of individual rights has led the Bank to meet - immediately after the judgment entered into force of *res judicata* - representatives of other social security bodies as well as the civil servants' administration, in order to propose the required legislative reforms during 2006. These reforms have become necessary in order to reconcile the need for workers' mobility with the principles of financial independence of the Bank and its functional autonomy.

Against this backdrop, it has been agreed that a draft law amending the law of 28 July 2000 coordinating the different pension schemes and any other texts dealing with individual pension rights and beneficiaries of the BCL's pension fund be prepared by the government department responsible for monitoring social security and submitted to the national legislator.

4.3 Buildings/facilities

Construction of the shell of the BCL's new building in the boulevard Prince Henri continued in 2005. In addition to work on the stone and glass façade, the installation of technical equipment also began.

The building will be completed on time, at the end of 2006, and on budget.

Concerning the Bank's main building, efforts in 2005 were mainly focused on the maintenance of the building and its facilities. Work was also carried out to ensure that its equipment and fittings comply with the legal requirements.

An analysis concerning health and security at the workplace has been undertaken together with the public service medical department.

4.4 Accounting and the budget

4.4.1 Accounting and finance

The BCL continued to strengthen its accounting system and its procedures in order to meet its internal quality standards and those of the Eurosystem. The Eurosystem requires the daily reporting of balance sheet data from each of its members according to harmonised rules.

The controlling systems in place proved to be effective during the year.

The Bank regularly checks the development of balance sheet, off-balance-sheet and profit and loss items. Investments, revenues and expenses are in particular closely monitored, with special attention paid to signing powers.

The cost accounting system gives an indication concerning costs and invoicing of services. The methodology follows the rules recommended by the Eurosystem. It consists of allocating BCL's operational expenses according to their destination, e.g. according to the respective sections and units, and it permits the costs of each of the Bank's activities to be determined.

The monthly balance sheet of the Bank is published on its internet site.

The management information system meets the need to follow the Bank's activities. It is based on a set of indicators, which are calculated daily, weekly, monthly, quarterly and annually. These tables include all activities of the Bank. The analysis of the profit and loss items is complemented by an analysis concerning the net profit of the various activities. The Bank strictly controls the development of the interest margin and compares the profitability of its investments to benchmarks.

The BCL regularly checks its risk exposure and monitors within this framework the appropriateness of own funds and of short-, middle- and long-term provisions. The Bank has adopted a prudent policy of constituting and maintaining provisions for general and specific bank risks.

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The Bank performs static and dynamic assessments of its long-term financial situation. It carries out prospective analyses of external factors like interest rates, exchange rates and other variables of the Eurosystem and of the economic situation.

The Bank's decision-making bodies are regularly informed of the results in order to be in a position to decide on future directions and actions to take.

The asset/liability committee closely follows the risk exposure and the financial situation during the year, and in particular the risk resulting from the appropriateness of assets and liabilities. It checks the investment limits imposed by the balance sheet positions of the NCB and the ECB.

4.4.2 Budget

Every year in December, the BCL's Council approves the budget for the coming year. The 2005 budget was drawn up in accordance with a budgetary procedure which aims to manage the Bank's resources in a rational manner.

The procedure ensures that the limit set when drawing up the budget will not be exceeded. Within this limit, expenses can be engaged only as far as they are in line with the Bank's rules regarding profitability and economic efficiency. The operational costs for 2005 have stayed within the budgetary limit approved by the Council.

All in all, it is important to underline that the BCL's budget reflects the Bank's corporate values, which are:

- professionalism
- quality in all its services
- stability provided by taking a long-term perspective
- objectivity resulting from the indiscriminating application of precise rules
- integrity resulting from the transparency of its internal operations and respect for professional ethics.

As regards the budget projections for 2006, a certain number of priorities have been identified during a reassessment of the BCL's objectives, notably: the formulation of an attractive vision for the Bank; the creation of a common orientation; the strengthening of the efficiency and a greater sense of individual responsibility; a streamlining of the organisational structure; and the mobilisation of the staff members' skills. All these priorities need to be further developed.

Finally, several options for centralising certain administrative tasks and for reorganising some internal resources have to be explored.

4.5 Internal audit activities

The BCL's internal control system is based on generally accepted standards prevailing in the financial sector and adapted to its activity as a central bank. The principles of internal control as well as the various responsibilities resulting thereof are described in the internal Manual of Procedures.

The main activity of the internal audit function is to assess the internal control system. The Internal Audit unit reports directly to the President of the Bank. The internal audit mission statement is based on the rules and regulations prevailing in the Luxembourg financial centre, as well as on the standards promoted by the Institute of Internal Auditors (IIA) and the ESCB Audit Policy.

The Internal Audit unit is in charge of the follow-up of the recommendations issued during its audit activities. Based on the annual internal audit plan which comprises audit engagements that are coordinated by the Internal Auditor's Committee at the level of the ESCB, as well as audit engagements at a national level, the Internal Audit unit carried out various reviews in 2005 in the fields of the Exchange Rate Mechanism (ERM) II, of the transport and storage of banknotes and coins, of statistical systems, and of telecommunication and information systems.

4. THE BCL AS AN ORGANISATION

4.6 Financial statements as at 31 December 2005

Preamble

Only the French version of the present financial statements has been reviewed by the Independent Auditor. Consequently, the financial statements only refer to the French version of the financial statements; other versions result from a conscientious translation made under the responsibility of the Board of Directors. In case of differences between the French version and the translation, the French version is binding.

4.6.1 Key figures as at year-end (in euro unless otherwise indicated)

	2004	2005	Variation en % 2005/2004
Total assets	34,795,519,545	43,907,910,680	26%
Banks' current accounts	5,063,321,077	6,810,321,790	35%
Claims on credit institutions	28,353,710,277	31,797,051,656	12%
Own funds (1), revaluation accounts, administrative provisions and specific banking risks	456,816,923	531,760,240	16%
Net result of banking activities (2)	81,998,162	84,434,406	3%
Total net revenues	36,851,687	42,335,991	15%
Administrative expenses	29,225,981	29,236,695	0%
Net profit	2,605,967	2,601,176	0%
Cash Flow (3)	56,200,003	74,824,801	33%
Personnel	206	203	-1%
BCL's part in the capital of the ECB	0.1568%	0.1568%	
BCL's part in the Eurosystem's monetary policy operations	8.213%	7.832%	

(1) Capital, reserves, provisions for general banking risks and net profit to be affected to the reserves.

(2) Net interest income, net result from fees and commissions, net result on financial operations.

(3) Net profit plus depreciation of tangible / intangible assets and write-downs on financial assets, as well as net transfers to administrative provisions and provisions for banking risks.

4.6.2 Report of the Independent Auditor

To the Council of the Banque centrale du Luxembourg

To the Government

To the Chamber of Deputies

We have audited the attached financial statements of the Banque centrale du Luxembourg for the year ended 31 December 2005. The financial statements are the responsibility of the Board of Directors and are approved by the Council. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the the Board of Directors, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the attached financial statements give, in conformity with the generally accepted accounting principles and those defined by the European System of Central Banks, a true and fair view of the financial position of the Banque centrale du Luxembourg as at 31 December 2005 and of the results of its operations for the year then ended.

DELOITTE S.A.
Réviseur d'entreprises

8 March 2006

Pascal Pincemin
Partner

Vafa Moayed
Partner

4. THE BCL AS AN ORGANISATION

4.6.3 Balance sheet as at 31 December 2005

	Note	2005 EUR	2004 EUR
ASSETS			
Gold and gold receivables	3	32,207,057	23,860,617
Claims on non-euro area residents denominated in foreign currency	4	203,694,972	218,661,158
- Receivables from the IMF		63,001,000	113,377,895
- Balances with banks, security investments, external loans and other external assets		140,693,972	105,283,263
Claims on euro area residents denominated in foreign currency	5	31,704,438	51,831,953
Claims on non-euro area residents denominated in euro	6	1,037,748,672	466,612,637
- Balances with banks, security investments and loans		1,037,748,672	466,612,637
Lending to euro area credit institutions related to monetary policy operations denominated in euro	7	31,796,282,172	28,353,620,150
- Main refinancing operations	7.1	24,611,000,000	21,478,000,000
- Long-term refinancing operations	7.2	7,185,139,250	6,875,620,150
- Marginal lending facility	7.5	142,922	0
Other claims on euro area credit institutions denominated in euro	8	769,484	90,127
Securities of euro area residents denominated in euro	9	1,678,903,325	1,463,985,126
Intra-Eurosystem claims	10	7,876,701,417	3,488,282,255
- Participating interest in ECB	10.1	9,660,235	9,660,235
- Claims related to the transfer of foreign reserves	10.2	87,254,014	87,254,014
- Other claims within the Eurosystem	10.3	7,779,787,168	3,391,368,006
Items in course of settlement		180	192
Other assets	11	1,249,898,963	728,575,330
- Tangible and intangible fixed assets	11.1	62,072,621	58,365,712
- Other financial assets	11.2	1,034,432,666	582,682,793
- Off-balance sheet instruments revaluation differences		0	607,500
- Accruals and prepaid expenses	11.3	108,605,281	60,940,395
- Sundry	11.4	44,788,395	25,978,930
Total assets		43,907,910,680	34,795,519,545

The accompanying notes form an integral part of the financial statements.

Balance sheet as at 31 December 2005 (continued)

	Note	2005 EUR	2004 EUR
LIABILITIES			
Banknotes in circulation	12	1,141,736,320	1,012,539,140
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	13	6,810,321,790	5,063,321,077
- Current accounts (covering the minimum reserve system)	13.1	6,810,321,790	5,063,321,077
Liabilities to other euro area residents denominated in euro	14	514,683,375	554,852,262
- General government	14.1	514,683,375	554,852,262
Liabilities to non-euro area residents denominated in euro	15	314,195,393	58,327,526
Liabilities to non-euro area residents denominated in foreign currency	16	47,455,312	51,854,230
Counterpart of special drawing rights allocated by the IMF	17	20,513,855	19,321,918
Intra-Eurosystem liabilities	18	34,202,831,350	27,341,616,355
- Net liabilities related to the allocation of euro banknotes within the Eurosystem	18.1	34,202,831,350	27,341,616,355
Items in course of settlement	19	9,735,110	3,947,631
Other liabilities	20	237,388,936	160,572,809
- Off-balance sheet instruments revaluation differences		1,205,990	664,000
- Accruals and income collected in advance		190,360,110	141,871,653
- Sundry		45,822,836	18,037,156
Provisions	21	412,064,679	355,941,192
Revaluation accounts	22	48,960,115	27,802,136
Capital and reserves	23	145,423,269	142,817,302
- Capital	23.1	25,000,000	25,000,000
- Reserves	23.2	120,423,269	117,817,302
Profit for the year		2,601,176	2,605,967
Total liabilities		43,907,910,680	34,795,519,545

The accompanying notes form an integral part of the financial statements.

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4.6.4 Off-balance sheet as at 31 December 2005

	Note	2005 EUR	2004 EUR
Custody deposits	24	145,773,541,714	132,113,030,126
Commitments and similar instruments	25	1,900,000,000	1,900,000,000
Foreign currency reserve assets managed on behalf of the ECB	26	92,352,754	76,187,489
Forward transactions	27	101,625,000	694,214,750
Numismatic collection		125,249	122,709
		147,867,644,717	134,783,555,074

4.6.5 Profit and loss account for the year 2005

	Note	2005 EUR	2004 EUR
Interest income	28	868,636,311	669,225,751
Interest expense	28	(779,311,460)	(585,693,474)
Net interest income	28	89,324,851	83,532,277
Realised gains / (losses) arising from financial operations	29	10,643,464	5,951,518
Write-downs on financial assets and positions	30	(15,693,001)	(7,422,706)
Transfer to/from provisions for foreign exchange rate and price risks	31	(46,032,505)	(41,498,079)
Net result of financial operations, write-downs and risk provisions		(51,082,042)	(42,969,267)
Fees and commissions income	32	9,723,673	7,648,934
Fees and commissions expense	32	(9,564,581)	(7,711,862)
Net result from fees and commissions	32	159,092	(62,928)
Income from participating interest	33	-	-
Net result of pooling of monetary income	34	(10,394,032)	(14,320,344)
Other income	35	14,328,122	10,671,948
Total net income		42,335,991	36,851,686
Staff costs	36	(18,753,866)	(17,858,894)
Other administrative expenses	37	(8,233,361)	(7,622,472)
Depreciation of tangible and intangible fixed assets	11.1, 38	(5,296,464)	(5,019,739)
Banknote production services	39	(714,270)	(497,560)
Other expenses	40	(6,736,854)	(3,247,054)
Profit for the year		2,601,176	2,605,967

The accompanying notes form an integral part of the financial statements.

4.6.6 Notes to the financial statements as at 31 December 2005

Note 1 - General

The Banque centrale du Luxembourg (BCL) was founded in accordance with the law of 22 April 1998. The Founding Law of 23 December 1998 stipulates that the main task of the BCL shall be to contribute to the accomplishment of the tasks of the European System of Central Banks (ESCB) so as to achieve the objectives of the ESCB. The BCL is a public institution, endowed with legal personality and financial independence.

Note 2 - Accounting policies

The accounting policies applied in preparing the financial statements are described below:

2.1 Layout of the financial statements

The financial statements of the BCL have been prepared and drawn up in accordance with the generally accepted accounting principles and the rules adopted by the ESCB.

2.2 Accounting principles

The following accounting principles have been applied:

- economic reality and transparency;
- prudence;
- recognition of post-balance-sheet events;
- accruals principle;
- consistency and comparability.

2.3 Basic principles

The financial statements are based on historical cost and are adjusted to take account of the valuation at market prices of securities, financial instruments, gold and of all the elements, both on-balance-sheet and off-balance-sheet, denominated in foreign currencies.

Transactions in financial assets and liabilities are reflected in the accounts of the BCL on their settlement date.

2.4 Gold, assets and liabilities in foreign currencies

Assets and liabilities denominated in foreign currencies (including gold) are converted into euro at the exchange rate in force on the balance sheet closing date. Income and expenses are converted at the exchange rate prevailing on the date of the transaction.

Foreign currencies are revalued on a currency-by-currency basis including on-balance-sheet and off-balance-sheet items.

Securities are revalued at market prices separately from the revaluation of foreign exchange for securities denominated in foreign currencies.

Gold is revalued on the basis of the euro price per fine ounce as derived from the quotation in US dollars established at the time of the London fixing on the last working day of the year.

2.5 Securities

Negotiable securities denominated in foreign currencies and in euro are valued at the market price prevailing on the balance sheet date. The revaluation took place item-by-item on the basis of their ISIN code.

2.6 Recognition of gains and losses

Income and expenses are assigned to the financial year during which they are earned or incurred.

Realised gains and losses on foreign exchange transactions, securities and financial instruments linked to interest rates and market prices are taken to the profit and loss account.

At the end of the year, unrealised revaluation gains on foreign currencies, securities and financial instruments are not considered in the profit and loss account, but transferred to a revaluation account on the liabilities side of the balance sheet.

Unrealised losses are recognised in the profit and loss account when they exceed previous revaluation gains registered in the corresponding revaluation account. They may not be reversed against new unrealised gains in subsequent years. Unrealised losses regarding a specific security, financial instrument, currency or in gold holdings are not netted with unrealised gains in other securities, financial instruments, currencies or gold holdings.

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In order to calculate the acquisition cost of securities or currencies that are sold, the average cost method is used on a daily basis. If any negative revaluation differences are taken to the profit and loss account, the average cost of the asset in question is adjusted downwards to the level of the current exchange rate or market price thereof.

For fixed-income securities, the premiums or discounts arising from the difference between the average acquisition cost and the redemption price are calculated and presented on a prorata basis as part of the interest positions and amortised over the remaining life of the securities.

2.7 *Post-balance-sheet events*

Assets and liabilities are adjusted to take account of events occurring between the balance sheet date and the date on which the BCL's Council approves the annual accounts if such events have a material effect on the assets and liabilities on the balance sheet date.

2.8 *Banknotes in circulation*

The European Central Bank (ECB) and the 12 national central banks (NCBs), which together comprise the Eurosystem, have issued euro banknotes as from 1 January 2002. The total value of euro banknotes in circulation is allocated on the last working day of each month in accordance with the banknote allocation key.

The ECB has been allocated a share of 8% of the total value of euro banknotes in circulation from 2002, whereas the remaining 92% has been allocated to NCBs according to their weightings in the capital key of the ECB. The share of banknotes allocated to each NCB is disclosed under the balance sheet liability item "Banknotes in circulation".

The difference between the value of the euro banknotes allocated to each NCB in accordance with the banknote allocation key and the value of the euro banknotes that it actually puts into circulation gives rise to remunerated intra-Eurosystem balances. These claims or liabilities, which incur interest, are disclosed under the sub-item "Intra-Eurosystem: Net claim/liability related to the allocation of euro banknotes within the Eurosystem".

From 2002 until 2007 the intra-system balances arising from the allocation of euro banknotes are adjusted in order to avoid significant changes in NCBs' relative income positions compared with previous years. The adjustments are effected by taking into account the differences between the average value of banknotes in circulation of each NCB in the period from July 1999 to June 2001 and the average value of banknotes that would have been allocated to them during that period under the ECB's capital key. The adjustments will be reduced in annual stages until the end of 2007; income on banknotes thereafter will be allocated fully in proportion to the NCBs' paid-up shares in the ECB's capital.

The interest income and expense on these balances is cleared through the accounts of the ECB and is disclosed under "Net interest income".

The Governing Council of the ECB has decided that the seigniorage income of the ECB, which arises from the 8% share of euro banknotes allocated to the ECB, shall not be distributed for 2005. This income has been allocated, in the ECB's accounts, to a provision for foreign exchange rate, interest rate and gold price risks.

2.9 *Intra-Eurosystem claims and liabilities*

Intra-Eurosystem balances arising from the allocation of euro banknotes within the Eurosystem are included as a net single asset or liability under "Net claim/liability related to the allocation of euro banknotes within the Eurosystem".

Intra-Eurosystem claims and liabilities arising from TARGET balances and counterparties accounts are shown as a single net asset or liability on the balance sheet.

2.10 Treatment of tangible and intangible assets

The tangible and intangible assets are recorded at their acquisition cost less depreciation. Depreciation was calculated on a straight-line basis over the expected economic lifetime of the assets:

	Years
Buildings	25
Renovation of buildings	10
Furniture and equipment	3-5
Computer hardware and software	4

2.11 Pension fund

As at 1 January 1999, after the entry into force of the Founding Law of 23 December 1998, the pension claims of the BCL's staff members are fully supported by the BCL. The pension fund aims to cover the risks related to ageing, infirmity and survival, was set up in 2000. The actuarial method for determining the BCL's liabilities towards its agents was approved by the pension fund's Management Committee as at 12 February 2001.

The actuarial method determines the pension fund's liability related to ageing, infirmity or survival for each agent. The model is based on each agent's personal and career data, on the level of inflation for the next 60 years as well as on an average rate of return generated by the fund's assets.

The BCL's liabilities related to pensions are shown in the account "Provisions for pensions". The provision increases as a result of regular transfers by the agent and by the BCL as employer. In addition, if necessary, periodic transfers from the account "Booking reserve of the pension fund", equivalent to the revenues generated by the fund's assets, to adjust the account "Provision for pensions" to its actuarial value are booked. In cases where transfers are insufficient cover the BCL's pension liabilities, the difference between the existing provision and the effective claim is covered by a special transfer to be supported by the BCL.

2.12 Provision for banking risks

The BCL's provision policy is intended to cover specific and general risks resulting from the Bank's activities.

Note 3 - Gold and gold receivables

As at 31 December 2005, the BCL held 2,063.73 ounces of fine gold amounting to €0.9 million (2,202.23 ounces of fine gold amounting to €0.7 million as at 31 December 2004) and a top-rated gold bond issued by the International Bank for Reconstruction and Development purchased in 2002 and valued at €31.3 million (€23.2 million as at 31 December 2004).

On the balance sheet date, gold is valued on the basis of the euro price per fine ounce derived from the quotation in US dollars established at the London fixing on 30 December 2005.

Note 4 - Claims on non-euro area residents denominated in foreign currency

	2005 EUR	2004 EUR
Receivables from the IMF	63,001,000	113,377,895
Balances with banks, security investments, external loans and other external assets	140,693,972	105,283,263
	203,694,972	218,661,158

Under this item are recorded the BCL's foreign exchange reserve holdings with counterparties situated outside the euro area (including international and supranational institutions and central banks that are not members of the Eurosystem).

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This item is broken down into two sub-items:

- receivables from the International Monetary Fund (IMF) are made up of reserve tranche position and SDR holdings. SDR are reserve assets created *ex nihilo* by the IMF and allocated by it to its members. A country's SDR holdings initially amount to the SDR allocated. Afterwards, SDR holdings are subject to fluctuations as a result of encashments and transactions with other SDR holders. The reserve tranche position corresponds to the net amount of the quota and the IMF's currency holding and takes into account the re-evaluation of the general account.
- balances held on accounts with banks outside the euro area as well as securities, loans and other foreign currency assets issued by non-residents of the euro area. This sub-item includes in particular the US dollar securities portfolio which could be used, if needed, for monetary policy operations.

This portfolio, which amounted to €71.7 million as at 31 December 2005 (€52.8 million as at 31 December 2004), only contains government bonds and top-rated bonds issued by international and supranational institutions denominated in US dollars. Securities are valued at market prices. As at 31 December 2005, their value at market prices included an unrealised loss amounting to €0.4 million (unrealised loss amounting to €0.2 million as at 31 December 2004).

Balances with banks amounted to €68.9 million as at 31 December 2005 (€52.5 million as at 31 December 2004).

Note 5 - Claims on euro area residents denominated in foreign currency

This item comprises BCL's balances denominated in foreign currency with counterparties inside the euro area.

Note 6 - Claims on non-euro area residents denominated in euro

	2005 EUR	2004 EUR
Balances with banks	6,711,897	589,696
Security investments	1,031,036,775	466,022,941
	1,037,748,672	466,612,637

This item contains balances held on accounts with banks outside the euro area as well as securities, loans and other euro-denominated assets issued by non-residents of the euro area.

This portfolio only contains government bonds and first rated bonds issued by companies outside the euro area denominated in euro. Securities are valued at market prices. As at 31 December 2005, their value at market prices included an unrealised loss amounting to €14.2 million (unrealised loss amounting to €4.9 million as at 31 December 2004).

Note 7 - Lending to euro area credit institutions related to monetary policy operations denominated in euro

This balance sheet item represents the liquidity-providing transactions executed by the BCL with Luxembourg credit institutions.

The item is divided into various sub-items depending on the type of instrument used to provide liquidity to the financial sector:

	2005 EUR	2004 EUR
Main refinancing operations	24,611,000,000	21,478,000,000
Longer-term refinancing operations	7,185,139,250	6,875,620,150
Fine-tuning reverse operations	-	-
Structural reverse operations	-	-
Marginal lending facility	142,922	-
Credits related to margin calls	-	-
	31,796,282,172	28,353,620,150

7.1 Main refinancing operations

This sub-item records the amount of liquidity provided to credit institutions by way of weekly one-week tenders.

7.2 Long-term refinancing operations

This sub-item records the amount of credit extended to credit institutions by way of monthly three-month tenders.

7.3 Fine-tuning reverse operations

This sub-item records open market operations carried out on a non-regular basis, intended primarily to meet unexpected fluctuations in market liquidity.

7.4 Structural reverse operations

These are open market operations carried out with the primary intention of bringing about a lasting change in the structural liquidity position of the financial sector vis-à-vis the Eurosystem.

No such transactions were made during the year under review.

7.5 Marginal lending facility

This sub-item records a standing facility enabling counterparties to obtain 24-hour credit from the Bank at a pre-specified interest rate, against eligible collateral.

7.6 Credits related to margin calls

This sub-item records additional credit extended to credit institutions and resulting from the increase in the value of the securities pledged as collateral for other credits extended to these same institutions.

No such operation took place during the year just ended.

Note 8 - Other claims on euro area credit institutions denominated in euro

This item includes the BCL's current accounts and fixed-term deposits not related to monetary policy operations with credit institutions inside the euro area.

Note 9 - Securities of euro area residents denominated in euro

This item covers the BCL's portfolio in euro issued by residents of the euro area which could be used, if needed, for monetary policy operations. This amounted to €1,679 million as at 31 December 2005 (€1,464 million as at 31 December 2004).

This portfolio only contains government bonds in euro issued by Member States of the European Union and first rated bonds issued by companies of the euro area. Securities are valued at market prices. As at 31 December 2005, their value at market prices included an unrealised loss amounting to €16.2 million (unrealised loss amounting to €1.5 million as at 31 December 2004).

Note 10 - Intra-Eurosystem claims

10.1 Participating interest in ECB

Pursuant to Article 28 of the ESCB Statute, the ESCB national central banks are the sole subscribers to the capital of the ECB. Subscriptions depend on shares which are fixed in accordance with Article 29.3 of the ESCB Statute and which are subject to adjustment every five years. The first such adjustment following the establishment of the ECB took effect on 1 January 2004. On 1 May 2004 a second change of the ECB's capital key followed as a result of the accession of ten Member States.

On 31 December 2005, the share that the BCL held in the capital of the ECB was 0.1568%, which amounted to €9,660,235, on a total of subscribed capital of the ECB of €5.565 billion (no change compared with 31 December 2004).

The share that the BCL held in the accumulated net profits of the ECB reflects the repayment of €0.9 million by the ECB.

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10.2 Claims equivalent to the transfer of foreign reserves

This sub-item represents the euro-denominated claims on the ECB in respect of the transfer of part of the BCL's foreign reserves. The claims are denominated in euro at a value fixed at the time of their transfer.

They are remunerated at the latest available marginal rate for the Eurosystem's main refinancing operations, adjusted to reflect a zero return on the gold component.

As at 31 December 2005, the claim of the BCL amounted to €87,254,014 (no change compared with 31 December 2004).

10.3 Other claims within the Eurosystem

This sub-item represents the BCL's net claims towards the Eurosystem, mostly from transactions resulting from cross-border payments initiated for monetary or financial operations, made via the TARGET system, between the BCL and the other national central banks as well as the ECB. This claim amounts to €7.8 billion as at 31 December 2005 (€3.4 billion as at 31 December 2004).

The net position vis-à-vis the ECB bears interest at the marginal interest rate applying to the main refinancing operations.

Note 11 - Other assets

11.1 Tangible and intangible assets

Tangible and intangible fixed assets developed as follows:

The sub-item "Buildings" comprises the acquisition cost of the premises located at 2, boulevard Royal, the costs incurred in relation to the reconstruction and fitting-out of the Pierre Werner building and the renovations made to the Siège Royal (main building). The building located on boulevard Prince Henri was completely written off in 2003, having been demolished in order to construct a new one. Construction started in 2004 and is progressing as expected.

The Pierre Werner building and the one on the boulevard Prince Henri are considered as new buildings and are being amortised over a period of 25 years while the costs incurred in relation to the transformation of the Siège Royal are considered as renovations and are being amortised over 10 years.

11.2 Other financial assets

The components of this item are as follows:

	2005 EUR	2004 EUR
Other participating interests	216,994	162,033
Pension fund	78,219,526	64,005,693
Securities portfolio	955,996,146	518,515,067
	1,034,432,666	582,682,793

The other participating interests comprise the entry fees in LIPS-Net and the BCL's investments in RTGS-L GIE, SWIFT and ATTF.

	Buildings EUR	Furniture and equipment EUR	Software EUR	Total EUR
Cost as at 1 January 2005	73,791,708	9,689,846	3,934,114	87,415,668
Disposals	-	(72,719)	-	(72,719)
Acquisitions	7,535,465	1,247,421	220,487	9,003,373
Cost as at 31 December 2005	81,327,173	10,864,548	4,154,601	96,346,322
Accumulated depreciation as at 1 January 2005	19,060,369	7,008,130	2,981,457	29,049,956
Disposals	-	(72,719)	-	(72,719)
Depreciation	3,396,806	1,349,845	549,813	5,296,464
Accumulated depreciation as at 31 December 2005	22,457,175	8,285,256	3,531,270	34,273,701
Net book value as at 31 December 2005	58,869,998	2,579,292	623,331	62,072,621

The assets of the pension fund are recorded in the accounts under "Pension fund BCL". The balance of this account corresponds to the net asset value of the fund as calculated by the depositary bank as at 31 December 2005.

The securities portfolio recorded under this heading corresponds to the securities held by the BCL for the purpose of the investment of own funds and amounts owed to third parties amounting to a total of €956.0 million (€518.5 million as at 31 December 2004). Securities are valued at market prices. As at 31 December 2005, their value at market prices included an unrealised gain amounting to €5.4 million (unrealised gain amounting to €14.0 million as at 31 December 2004).

11.3 Accruals and prepaid expenses

Most of this item consists of the accrued interests on monetary policy operations, securities and receivables from the IMF.

Are also included under this item are the commissions receivables, prepaid expenses (including salaries paid for January 2006) and other income receivable.

11.4 Sundry

	2005 EUR	2004 EUR
Withdrawals in advance	9,735,000	3,947,500
Others	35,053,395	22,031,430
	44,788,395	25,978,930

The sub-item "Withdrawals in advance" corresponds to the amount of euro banknotes ordered by the credit institutions as at 31 December 2005 and which were not put into circulation by that date.

The sub-item "Others" consists mainly of the counterpart of the unrealised loss on SDR recorded in the financial statements of the BCL which is guaranteed by the State according to the agreement signed in May 1999 establishing the financial relationship between the State of Luxembourg and the BCL as well as a claim in relation to the pension fund.

Note 12 - Banknotes in circulation

This item includes the BCL's share of the total euro banknotes put into circulation by the 12 central banks of the Eurosystem according to their weightings in the capital of the ECB, which totalled €1,141,7 million (€1,012,5 million as at 31 December 2004).

Note 13 - Liabilities to euro area credit institutions related to monetary policy operations denominated in euro

	2005 EUR	2004 EUR
Current accounts (covering the minimum reserves)	6,810,321,790	5,063,321,077
Deposit facility	-	-
Fixed-term deposits	-	-
Fine-tuning reverse operations	-	-
Deposits related to margin calls	-	-
	6,810,321,790	5,063,321,077

This item primarily comprises credit institutions' accounts held within the framework of the requirements of the minimum reserve system.

13.1 Current accounts (covering the minimum reserves)

This sub-item records accounts denominated in euro of credit institutions which mainly serve to meet minimum reserve requirements. These requirements have to be respected over an average unsettled period starting the Wednesday following the Governing Council's meeting to set the interest rate.

13.2 Deposit facility

This sub-item records the standing facility allowing credit institutions to make 24-hour deposits with the Bank at a pre-specified interest rate.

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13.3 Fixed-term deposits

This sub-item records deposits made at the Bank for the purpose of absorbing market liquidity in connection with fine-tuning operations in the Eurosystem.

13.4 Fine-tuning reverse operations

This sub-item records other monetary policy operations aimed at tightening liquidity.

No such operation took place in 2005.

13.5 Deposits related to margin calls

This sub-item records deposits made by credit institutions to compensate for the decrease in the value of securities pledged as collateral for other credits granted to these same institutions.

No such operation took place in 2005.

Note 14 - Liabilities to other euro area residents denominated in euro

14.1 Liabilities to general government

This item records the amounts owed to the Luxembourg Treasury as follows:

	2005 EUR	2004 EUR
Current account	567,560	597,552
Account related to euro coins issued by the Treasury	124,115,815	104,254,710
Fixed-term deposit	390,000,000	450,000,000
	514,683,375	554,852,262

In accordance with the amendment of 10 April 2003 to the agreement between the State of Luxembourg and the BCL establishing their financial relationship, the "Account related to euro coins issued by the Treasury" corresponds to the amount of coins issued by the BCL in the name and for the account of the Treasury.

The fixed-term deposit relates to the agreement between the State of Luxembourg and the BCL which originally specified that the State should maintain at the BCL a deposit equivalent to the BCL's claim on the National Bank of Belgium in relation to Belgian banknotes circulating in Luxembourg. The fixed-term deposit matured on 1 March 2002 and was replaced, following agreement between parties, by a term deposit renewed on a monthly basis.

In order to strengthen the BCL's own funds and in accordance with the articles of the agreement which foresee this possibility, the State waived the remuneration of its term deposit. The related income, amounting to €4.3 million (€4.9 million as at 31 December 2004), is recorded under "Other income".

Note 15 - Liabilities to non-euro area residents denominated in euro

This item includes current accounts held by central banks, international and supranational institutions and other account holders outside the euro area.

Note 16 - Liabilities to non-euro area residents denominated in foreign currency

This item includes current accounts in foreign currency held by central banks outside the euro area.

Note 17 - Counterpart of special drawing rights allocated by the IMF

The amount shown under this item represents the countervalue of the SDR, converted to euro at the same rate as applied to the SDR assets, which should be returned to the IMF if the SDR are cancelled, if the SDR Department established by the IMF is closed or if Luxembourg decides to withdraw from it. This liability, of unlimited duration, amounts to SDR 17.0 million, or €20.5 million as at 31 December 2005 (SDR 17.0 million, or €19.3 million as at 31 December 2004).

Note 18 - Intra-Eurosystem liabilities

18.1 Net liabilities related to the allocation of euro banknotes within the Eurosystem

This item consists of the liabilities of the BCL vis-à-vis the Eurosystem relating to the allocation of euro banknotes within the Eurosystem. The net position bears interest at the marginal interest rate applying to the main refinancing operation.

Note 19 - Items in course of settlement

This item contains mainly the counterpart of the euro banknotes ordered by credit institutions as at 31 December which were not put into circulation by that date.

Note 20 - Other liabilities

This item comprises mainly the negative revaluation differences on financial instruments linked to interest rates and market prices, accrued interest, including accrued interest on intra-Eurosystem liabilities, as well as miscellaneous expenses payable, including suppliers, and the Luxembourg banknotes not yet returned.

The Luxembourg banknotes still circulating as at 31 December 2005 amount to €5.6 million (€5.8 million as at 31 December 2004).

Note 21 - Provisions

The provisions are as follows:

	2005 EUR	2004 EUR
Provisions for banking risks	327,182,153	281,149,648
Provisions for pensions	79,680,870	71,758,670
Other provisions	5,201,656	3,032,874
	412,064,679	355,941,192

21.1 Provisions for banking risks

Provisions for banking risks include the following items:

	2005 EUR	2004 EUR
Provision covering credit risk	141,982,925	112,937,113
Provision covering operational risk	11,150,000	13,000,000
Provision covering liquidity risk	13,523,377	11,658,367
Provision covering interest rate risk	200,000	200,000
	166,856,302	137,795,480
Provisions for general banking risks		
Provision for liabilities resulting from monetary agreements	32,341,954	32,341,954
Other provision for general banking risks	127,983,897	111,012,214
	160,325,851	143,354,168
	327,182,153	281,149,648

21.1.1 Provision covering credit risk

The provision for €142.0 million (€112.9 million as at 31 December 2004) corresponds to:

- 4% of the BCL's own securities portfolio existing as at 31 December 2003 and still kept as at 31 December 2005 (portfolio allocated to monetary policy operations if necessary and structural portfolio) and participations other than the participating interest in the ECB;
- 2% of the increase between 31 December 2003 and 31 December 2005 of the BCL's own securities portfolio and participations other than the participating interest in the ECB;

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- 4% of the total amount lent by the Eurosystem as at year-end for monetary policy reasons multiplied by the capital key corresponding to the BCL (0.21933 %).

The BCL's aim is to attain a rate of 4% on all items in the medium term.

21.1.2 Provision covering operational risk

This provision is intended to cover the risk of losses resulting from an inadequacy or fault attributable to procedures, to the human factor or to the BCL's systems or to external causes. Because of a lack of relevant statistics on the dimension of risk, the transfer to the provision is based on the Basic Indicator Approach described in the consultative working paper of the Basel Committee as being 15% of the average for the last three years of the net banking product (including payments allocated on monetary income).

21.1.3 Provision for liabilities resulting from monetary agreements

The provision for liabilities resulting from monetary treaties was initially created in 1984 by the Institut Monétaire Luxembourgeois (IML) together with the Ministry of Treasury in order to face any future monetary liabilities.

In 2004, the Bank reversed €3 million of this provision to cover the BCL's participation in the ECB's loss for the accounting year 2004.

21.1.4 Other provision for general banking risks

In 2005, for prudence's sake and to safeguard its assets, the BCL transferred €17.0 million (€17.9 million for the financial year 2004) to the provision for general banking risks to cover any inherent risks related to central bank activities.

21.2 Provisions for pensions

Provisions for pensions include the following items:

	2005 EUR	2004 EUR
Provision for pensions	77,289,000	69,366,800
Provision for equalisation and financial risks	850,252	850,252
Provision for increase of PBO	1,541,618	1,541,618
	79,680,870	71,758,670

21.2.1 Provision for pensions

The pensions claims of its agents are fully supported by the BCL. The corresponding liability is calculated on the basis of the actuarial method described in note 2.11 in consideration of current factors and amounted to €77.3 million as at 31 December 2005 (€69.4 million as at 31 December 2004).

The increase of the provision during the year results from:

- monthly deductions from the gross salaries of BCL agents (employee's part) as well as the employer's share;
- periodic transfers from the account "Booking reserve of the pension fund" to adjust the account "Provision for pensions" to its actuarial value;
- a transfer, if needed, to adjust the account "Provision for pensions" to its actuarial value.

In 2001 and according to Article 35 paragraph 4(c) of its Founding Law, the BCL made an exceptional transfer from its reserves in order to adjust the pension fund to the required amount as at 31 December 2001. In addition, Article 35 paragraph 4(a) of the same law states that "the Luxembourg pension funds that received contributions from persons that are or become BCL agents shall pay these amounts into the BCL's pension fund".

At the date of this Annual Report, Luxembourg pension funds had not paid the contributions as stipulated in Article 35 paragraph 4(a). Consequently, the exceptional transfer from the reserves in 2001, amounting to €33.8 million, was determined without considering the claim on the pension funds, which will be used for the reconstitution of the reserves.

21.2.2 Provision for equalisation and financial risks

A provision of €3 million for equalisation and financial risks was set up in 2001 to cover fluctuations in the pension fund's liabilities in its early years and/or to compensate for a lower return on assets. In 2002, the provision was used to the amount of €2.1 million. The provision has not changed since then.

21.2.3 Provision for increase of Projected Benefit Obligation

The provision of €1.5 million (same figure as at 31 December 2004) is based on the average expense in relation to pensions, disability and death for new agents who belong to the BCL's staff or are included in the budgeted figures for 2005 but are not included in the pension fund's liabilities calculation as at 31 December 2005. The liability (Projected Benefit Obligation or PBO) equals the potential payments at their present value taking into account individual parameters and the actuarial method used.

21.3 Other provisions

A provision of €5.2 million (€3.0 million as at 31 December 2004) has been created in relation to the difference between the amount of a claim of the BCL's pension fund against the Luxembourg pension funds as decided by the *Cour d'Appel* (following the BCL's judicial proceedings). The *Cour d'Appel's* decision has not been subject to appeal at the *Cour de Cassation*. The amount booked has been determined according to the rules which govern the future financial relationship between the BCL and the Luxembourg pension funds (see Note 35).

The provision of €3.0 million set up by the BCL in 2004 to offset the ECB's loss was used following the decision taken by Governing Council at its meeting on 17 March 2005.

Note 22 - Revaluation accounts

This item includes positive revaluation differences related to the spread between the exchange rate as at year-end and the average exchange rate of the BCL's currency and gold positions, as well as positive revaluation differences related to the spread between the market value as at year-end and the amortised cost for securities positions.

Note 23 - Capital and reserves

23.1 *Capital*

The State of Luxembourg is the sole shareholder of the BCL's capital, which is fixed at €25 million euro.

23.2 *Reserves*

The reserves amount to €120.4 million (€117.8 million as at 31 December 2004). This amount was increased by €2.6 million in 2005 following the allocation of profit for 2004 according to the decision of the BCL's Council and its Founding Law (Article 31).

Note 24 - Custody deposits

This item includes the securities given into custody by Luxembourg credit institutions to cover their liabilities related to refinancing operations, marginal lending facilities and intra-day credits.

This item also includes the securities given into custody in Luxembourg and used as a guarantee by commercial banks incorporated in other Member States according to the Correspondent Central Banking Model (CCBM). This agreement allows commercial banks to obtain funding from their country of residence's central bank by using the securities held in another Member State as a guarantee.

As at 31 December 2005, the market value of these securities amounted to €145.8 billion (€132.1 billion as at 31 December 2004).

Note 25 - Commitments and similar instruments

	2005 EUR	2004 EUR
Commitments and similar instruments	1,900,000,000	1,900,000,000

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This item corresponds to the guarantee issued by the BCL for the night-time link project. This commitment is guaranteed by assets received in custody for the same amount.

Note 26 - Foreign currency reserve assets administrated on behalf of the ECB

This item includes the foreign currency reserves at market value managed by the BCL on behalf of the ECB.

Note 27 - Forward contracts

The BCL is engaged in bond and stock index futures. These instruments are mainly held for hedging purposes of interest rate risks related to the securities portfolio and for the purpose of adjusting the duration of the existing portfolio depending on market conditions.

As at 31 December 2005, the total liabilities related to these forward contracts amounted to €101.6 million (€694.2 million as at 31 December 2004). One security has been given as a guarantee in order to cover the initial margin deposit. This security remains on the BCL's balance sheet for an amount of €5.0 million as at 31 December 2005 (€5.2 million as at 31 December 2004).

Note 28 - Net interest income

This item includes interest income, after deduction of interest expense, on assets and liabilities in foreign currency and in euro. Interest income and expense are as follows:

Composition of interest income

	Amounts in foreign currency		Amounts in euro	
	EUR		EUR	
	2005	2004	2005	2004
IMF	2,394,911	2,201,200	-	-
Monetary policy	-	-	622,542,527	537,611,506
Intra-Eurosystem claims	-	-	148,403,622	67,627,565
Securities	2,762,511	846,835	89,498,935	59,758,435
Gold	406,745	371,258	-	-
Other	2,537,122	667,778	89,938	141,174
Total	8,101,289	4,087,071	860,535,022	665,138,680

Composition of interest expense

	Amounts in foreign currency		Amounts in euro	
	EUR		EUR	
	2005	2004	2005	2004
IMF	(529,901)	(368,866)	-	-
Current accounts (including minimum reserves) and deposits related to monetary policy operations	-	-	(146,465,831)	(136,206,536)
Liabilities related to the reallocation of euro banknotes in the Eurosystem	-	-	(625,344,817)	(441,887,406)
Other intra-Eurosystem liabilities	-	-	(26,768)	(919,153)
Interests on term deposits	-	-	(4,284,514)	(869,228)
Other liabilities	(1,707,550)	(538,813)	(952,079)	(713,961)
Total	(2,237,451)	(907,679)	(777,074,009)	(584,785,795)

The increase in interest results from an increase in amounts outstanding rather than from a change in the interest rates.

Note 29 - Realised gains / (losses) arising from financial operations

This item includes the result from transactions in foreign currencies, from securities and from financial instruments linked to interest rates and market prices, i.e. gains realised minus loss realised on these transactions. In 2005, they amounted to €17.4 million (€15.4 million as at 31 December 2004) and to €6.8 million (€9.4 million as at 31 December 2004) respectively, making a net income of €10.6 million (€6.0 million as at 31 December 2004).

Note 30 - Write-downs on financial assets and positions

This item includes revaluation losses on securities for €15.5 million and on financial instruments linked to interest rates and market prices for €0.2 million in 2005 (€0.7 million and €0.7 million respectively plus €6.0 million on foreign currencies in 2004).

Note 31 - Transfer to/from provisions for foreign exchange rate and price risks

This item includes the transfers to and from provisions for banking risks.

Note 32 - Net result from fees and commissions

Fees and commissions income and expense are as follows:

	Fees and commissions income		Fees and commissionsexpense	
	EUR		EUR	
	2005	2004	2005	2004
Securities	9,119,748	7,309,392	(9,488,128)	(7,610,313)
Others	603,925	339,542	(76,453)	(101,549)
Total	9,723,673	7,648,934	(9,564,581)	(7,711,862)

Note 33 - Income from participating interest

This item may include the dividend distributed by the European Central Bank.

No dividend was distributed in 2005.

In 2005, the ECB's income on euro banknotes in circulation amounting to €868 million was used in full by the ECB in accordance with a decision of the Governing Council with respect to the establishment of a provision for foreign exchange rate, interest rate and gold price risks.

Note 34 - Net result of pooling of monetary income

Since 2003, the monetary income of each Eurosystem NCB is determined by measuring the actual annual income that derives from the earmarkable assets held against its liability base. The liability base consists of the following items:

- banknotes in circulation;
- liabilities to credit institutions related to monetary policy operations denominated in euro;
- net intra-Eurosystem liabilities resulting from TARGET transactions;
- net intra-Eurosystem liabilities related to the allocation of euro banknotes within the Eurosystem.

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Any interest paid on liabilities included within the liability base is to be deducted from the monetary income to be pooled.

The earmarkable assets consist of the following items:

- lending to euro area credit institutions related to monetary policy operations denominated in euro;
- intra-Eurosystem claims equivalent to the transfer of foreign reserve assets to the ECB;
- net intra-Eurosystem claims resulting from TARGET transactions;
- net intra-Eurosystem claims related to the allocation of euro banknotes within the Eurosystem;
- a limited amount of each NCB's gold holdings in proportion to its capital key.

Gold is considered as generating no income.

Where the value of an NCB's earmarkable assets exceeds or falls short of the value of its liability base, the difference shall be offset by applying to that difference the average rate of return on the earmarkable assets of all NCBs taken together.

The monetary income pooled by the Eurosystem is allocated among NCBs according to the subscribed capital key (0.21933% for the BCL).

Calculation of net monetary income allocated to the BCL:

	(EUR millions)	
	2005	2004
Monetary income pooled by BCL	(31.9)	(29.2)
Monetary income reallocated to BCL	21.5	17.9
Retained monetary income by the ECB	0.0	(3.0)
Net result arising from the calculation of monetary income	(10.4)	(14.3)

Note 35 - Other income

Other income includes revenues for €4.3 million (€4.9 million for 2004) that reflect the waiving by the State of Luxembourg of the interest due for 2005 on its term deposit with the BCL (see also Note 14.1) and the remuneration of the claim on the Luxembourg pension funds and reimbursement of amounts taken into account by the BCL for the Luxembourg pension funds for the years 2001 to 2005 for €5.2 million (€0 million in 2004).

This item also includes revenues for services rendered to third parties, transfers from administrative provisions and income from numismatic activities.

Note 36 - Staff costs

This item includes the salaries and compensations as well as the employer's share of contributions to the pension and social security schemes. The compensations paid to the Board of Directors amounted to €472,927 for the year 2005 (€456,830 for the year 2004).

As at 31 December 2005, the BCL employed 203 persons (206 as at 31 December 2004). The average number of persons working for the BCL from 1 January to 31 December 2005 was 206 (205 for the year 2004).

Note 37 - Administrative expenses

This item includes all general and recurring expenses, meaning rents, cleaning and repair of buildings and equipment, small goods and materials, fees paid and other services and supplies as well as training expenses. The compensations paid to the members of the Council amounted to €71,082 in 2005 (€68,237 in 2004).

Note 38 - Depreciation of tangible and intangible fixed assets

This item shows the depreciation applied on buildings, renovations on buildings, furniture and office equipment, computer hardware and software.

Note 39 - Banknote production services

This item shows mainly the costs related to the production and issue of banknotes denominated in euro.

Note 40 - Other expenses

The bulk of other expenses are related to the transfer to the administrative provisions (see Note 21.3) and costs related to numismatic activities.

