# AS SMP Bank

Bank's separate and consolidated
financial statements for the year ended
31 December 2011

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## MANAGEMENT REPORT

Dear shareholders and customers,

The Board of AS SMP Bank announces that the Bank has concluded 2011 successfully and during 2011 the Bank has continued developing its range of financial services, expanding its operating activities abroad. We are content that the positive results supplement the achievements of our country during the economic recovery process that should be highly appreciated as Latvia has achieved these results in circumstances when the global economy and international financial system faces one of the most difficult development phases.

Coordinating the Bank's operations and its development during the reporting period, the Bank has used the opportunities offered by the recovery process of economy purposefully at the same time assessing the potential risks and taking measures in order to decrease those. The programme implemented by the Bank to support the operating activities of its customers during the crisis has yielded positive results and it is possible to plan the financial resources for further development of the projects already commenced.

The new financial services of the Bank (e-business, SMS messages about customer's transactions and account status, new POS terminals for card settlements in the stores etc.) attract more and more customers. It should be noted in particular that the extended range of payment card services provided by the Bank includes not only the opportunity to personalize payment cards in a short period of time in Latvia and Lithuania but also opportunities to receive these services at reduced prices in the territory of Latvia, Lithuania and Russian Federation. As a result, from the operations and results of the Lithuanian branch of the Bank opened in 2011 it can be concluded that high quality financial services even today help enter new financial services markets used by other players for a long time.

At the same time the Bank is constantly increasing the security of its services and takes timely measures to protect customer transactions and personal information. Therefore the Bank has started using higher security level payment cards (with DDA chips) and obtained the licence to use increased security system (3D Secure) to provide the services of internet merchants.

The Bank highly appreciates its customers' loyalty and mutually beneficial long-term cooperation that allows looking forward with hope and contributing to the recovery process of our economy. The Bank acknowledges that it will continue to be an experienced, safe and stable partner for its customers and business partners.

Best regards,

Svetlana Dzene,
Chairperson of the Board
27 March 2012

## INFORMATION ON THE BANK'S MANAGEMENT

**Council members as at the date of signing these financial statements**

| Name, surname | Position | Date of appointment |
|---|---|---|
| Dmitry Kalantirsky | Chairman of the Council | 12 October 2006 |
| Artem Obolensky | Council Member | 12 October 2006 |
| Andris Dzenis | Council Member | 12 November 2006 |
| Arkady Rotenberg | Council Member | 12 October 2006 |
| Boris Rotenberg | Council Member | 12 October 2006 |

There were no changes in the Council in 2011.

**The Board members as at the date of signing these financial statements**

| Name, surname | Position | Date of appointment |
|---|---|---|
| Svetlana Dzene | Chairperson of the Board | 28 September 1995 |
| Maija Treija | Board Member | 18 July 2005 |
| Natālija Prohorova | Board Member | 10 March 1995 |
| Ivars Lapiņš | Board Member | 19 March 1999 |
| Sergejs Golubčikovs | Board Member | 27 June 2005 |
| Dmitrijs Kozlovs | Board Member | 22 October 2010 |
| Irina Cibuļonoka | Board Member | 8 November 2011 |

On 8 November 2011, Irina Cibuļnoka was appointed to the Board.

## STATEMENT OF THE MANAGEMENT'S RESPONSIBILITIES

AS SMP Bank (hereinafter – Bank) management is responsible for the preparation of the consolidated financial statements of the Bank and its subsidiary AS SMP Finance (hereinafter – Group as well as for the preparation of the financial statements of the Bank.

The financial statements on pages 8 to 65 are prepared based on source documents and present fairly the financial position of the Group and the Bank as at 31 December 2011 and the results of its operations and cash flows for the year ended 31 December 2011.

The above mentioned consolidated and Bank's financial statements are prepared in accordance with the International Financial Reporting Standards, as adopted by the European Union. Appropriate accounting policies have been applied on a consistent basis. Prudent and reasonable judgments and estimates have been made by the Management in the preparation of the financial statements.

The management of AS SMP Bank is responsible for the maintenance of a proper accounting system, safeguarding the Group's and the Bank's assets, and prevention and detection of fraud and other irregularities in the Group and the Bank. They are also responsible for operating the Bank in compliance with the Law on Credit Institutions, regulations of the Finance and Capital Markets Commission and other legislation of the Republic of Latvia applicable to credit institutions.

On behalf of the Board and Council:

D. Kalantirskijs
Chairman of the Council

S. Dzene
Chairperson of the Board

27 March 2012

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# Independent Auditors' Report

## To the shareholders of AS "SMP Bank"

### Report on the Separate and Consolidated Financial Statements

We have audited the accompanying separate financial statements of AS "SMP Bank" ("the Company"), which comprise the separate statement of financial position as at 31 December 2011, the separate statements of comprehensive income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages 8 to 65. We have also audited the accompanying consolidated financial statements of AS "SMP Bank" and its subsidiaries ("the Group"), which comprise the consolidated statement of financial position as at 31 December 2011, the consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages 8 to 65.

*Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these separate and consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the European Union and for such internal controls as management determines are necessary to enable the preparation of these financial statements that are free from material misstatement, whether due to fraud or error.

*Auditors' Responsibility*

Our responsibility is to express an opinion on these separate and consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether these financial statements are free of material misstatement.

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

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

*Opinion*

In our opinion, the separate financial statements give a true and fair view of the financial position of AS "SMP Bank" as at 31 December 2011, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of AS "SMP Bank" and its subsidiaries as at 31 December 2011, and of the consolidated financial performance and consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

## Report on Other Legal and Regulatory Requirements

In addition, our responsibility is to assess whether the accounting information included in the Management Report, as set out on page 3, the preparation of which is the responsibility of the Management, is consistent with the separate and consolidated financial statements. Our work with respect to the Management Report was limited to the aforementioned scope and did not include a review of any information other than drawn from the separate and consolidated financial statements of the Bank and Group. In our opinion, the management report is consistent with the financial statements.

Ondrej Fikrle
Partner pp KPMG Baltics SIA
Riga, Latvia
27 March 2012

Inga Lipšāne
Sworn Auditor
Certificate No 112

*This report is an English translation of the original Latvian. In the event of discrepancies between the two reports, the Latvian version prevails.*

## BANK'S SEPARATE AND CONSOLIDATED STATEMENT OF FINANCIAL POSITION

| ASSETS | Note | 2011 Group LVL '000 | 2011 Bank LVL '000 | 2010 Group LVL '000 | 2010 Bank LVL '000 |
|---|---|---|---|---|---|
| Cash and due from the Bank of Latvia | 6 | 11,106 | 11,106 | 11,390 | 11,390 |
| Demand deposits with credit institutions | 7 | 45,883 | 45,883 | 46,265 | 46,265 |
| Latvian government debt securities with fixed income | 8 | 3,498 | 3,498 | 3,103 | 3,103 |
| Fixed income debt securities | 9 | 2,553 | 2,553 | - | - |
| Loans and receivables | | 77,630 | 81,335 | 66,429 | 67,997 |
| *Loans and term deposits with credit institutions* | 10 | *7,145* | *7,145* | *5,386* | *5,386* |
| *Loans* | 11 | *70,485* | *74,190* | *61,043* | *62,611* |
| Financial assets held for trading: | | 35 | 35 | 20 | 20 |
| *Non-fixed income securities* | | *35* | *35* | *20* | *20* |
| Property and equipment | 12 | 743 | 675 | 721 | 721 |
| Investment property | 13 | 3,331 | - | 1,515 | - |
| Other tax assets | | 4 | 4 | 58 | 4 |
| Other assets | 14 | 324 | 250 | 471 | 464 |
| Assets held for sale | 15 | 373 | - | - | - |
| **Total assets** | | **145,480** | **145,339** | **129,972** | **129,964** |

The accompanying notes on pages 13 to 65 form an integral part of these Bank's separate and consolidated financial statements.

The Bank's separate and consolidated financial statements as set out on pages 8 to 65 were authorised for issue by Board and Council on 27 March 2012.

D. Kalantirskijs
Chairman of the Council

S. Dzene
Chairperson of the Board

## BANK'S SEPARATE AND CONSOLIDATED STATEMENT OF FINANCIAL POSITION

| LIABILITIES | Note | 2011 Group LVL '000 | 2011 Bank LVL '000 | 2010 Group LVL '000 | 2010 Bank LVL '000 |
|---|---|---|---|---|---|
| Due on demand to credit institutions | 16 | 275 | 275 | 8,974 | 8,974 |
| Financial liabilities carried at amortized cost: | | 132,959 | 132,971 | 102,415 | 102,469 |
| *Customers' deposits* | 17 | *130,180* | *130,192* | *101,415* | *101,469* |
| *Subordinated liabilities* | 18 | *2,779* | *2,779* | *1,000* | *1,000* |
| Other liabilities | 19 | 2,956 | 2,829 | 9,863 | 9,791 |
| Other taxes and social contributions | | 40 | 8 | 18 | 18 |
| Deferred tax liability | 28 | 24 | 24 | 23 | 23 |
| Corporate income tax | 28 | 86 | 86 | - | - |
| Provisions | 20 | 102 | 101 | 97 | 97 |
| **Total liabilities** | | **136,442** | **136,294** | **121,390** | **121,372** |
| | | | | | |
| **Capital and reserves** | | | | | |
| Share capital | 21 | 8,006 | 8,006 | 8,006 | 8,006 |
| Share premium | | 182 | 182 | 182 | 182 |
| Reserve capital | 21 | 105 | 105 | 105 | 105 |
| Retained earnings | | 719 | 752 | 265 | 299 |
| Total capital attributable to equity holders of the Group | | **9,012** | **9,045** | **8,558** | **8,592** |
| Non-controlling interest | | **26** | **-** | **24** | **-** |
| **Total equity** | | **9,038** | **9,045** | **8,582** | **8,592** |
| **Total liabilities and shareholders' equity** | | **145,480** | **145,339** | **129,972** | **129,964** |
| | | | | | |
| **Contingent liabilities** | 32 | **13,439** | **13,439** | **7,487** | **7,251** |

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The Bank's separate and consolidated financial statements as set out on pages 8 to 65were authorised for issue by Board and Council on 27 March 2012.

D. Kalantirskijs
Chairman of the Council

S. Dzene
Chairperson of the Board

## BANK'S SEPARATE AND CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

| | Note | 2011 Group LVL '000 | 2011 Bank LVL '000 | 2010 Group LVL '000 | 2010 Bank LVL '000 |
|---|---|---|---|---|---|
| Interest income | 22 | 3,300 | 3,244 | 2,948 | 2,879 |
| Interest expense | 23 | (1,196) | (1,196) | (1,435) | (1,435) |
| **Net interest income** | | **2,104** | **2,048** | **1,513** | **1,444** |
| Commission and fee income | 24 | 2,417 | 2,398 | 2,058 | 2,036 |
| Commission and fee expense | 25 | (509) | (509) | (399) | (399) |
| **Net commission income** | | **1,908** | **1,889** | **1,659** | **1,637** |
| Gain on trading with financial instruments, net | 26 | 1,329 | 1,306 | 950 | 936 |
| Other operating expenses | | (31) | (30) | (8) | (25) |
| **Net operating income** | | **5,310** | **5,213** | **4,114** | **3,992** |
| Administrative expenses | 27 | (3,841) | (3,747) | (3,373) | (3,324) |
| Net impairment allowance expense | 11 | (927) | (927) | (665) | (665) |
| **Profit before tax** | | **542** | **539** | **76** | **3** |
| Corporate income tax | 28 | (86) | (86) | - | - |
| **Profit for the period** | | **456** | **453** | **76** | **3** |
| **Attributable to:** | | | | | |
| *Equity holders of the Bank* | | *454* | *453* | *36* | *3* |
| *Non-controlling interest* | | *2* | - | *40* | - |
| **Total comprehensive income** | | **456** | **453** | **76** | **3** |
| **Attributable to:** | | | | | |
| *Equity holders of the Bank* | | *454* | *453* | *36* | *3* |
| *Non-controlling interest* | | *2* | - | *40* | - |

The accompanying notes on pages 13 to 65 form an integral part of these Bank's separate and consolidated financial statements.

The Bank's separate and consolidated financial statements as set out on pages 8 to 65 were authorised for issue by Board and Council on 27 March 2012.

D. Kalantirskijs
Chairman of the Council

S. Dzene
Chairperson of the Board

## BANK'S SEPARATE AND CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

| **Group**<br>**LVL '000** | **Share capital** | **Share premium** | **Reserve capital** | **Retained earnings** | **Total equity attributable to the Bank's shareholders** | **Non-controlling interest** | **Total equity** |
|---|---|---|---|---|---|---|---|
| **31 December 2009** | **7,006** | **182** | **105** | **229** | **7,522** | **(16)** | **7,506** |
| Total comprehensive income | | | | | | | |
| (Loss) / profit of the year | - | - | - | 36 | **36** | 40 | **76** |
| Transactions with shareholders, recorded directly in equity | | | | | | | |
| Share capital increase | 1,000 | - | - | - | **1,000** | - | **1,000** |
| **31 December 2010** | **8,006** | **182** | **105** | **265** | **8,558** | **24** | **8,582** |
| Total comprehensive income | | | | | | | |
| Profit for the year | - | - | - | 454 | **454** | 2 | **456** |
| **31 December 2011** | **8,006** | **182** | **105** | **719** | **9,012** | **26** | **9,038** |

| **Bank**<br>**LVL '000** | **Attributable to equity holders of the Bank**<br>**Share capital** | **Share premium** | **Reserve capital** | **Retained earnings** | **Total equity** |
|---|---|---|---|---|---|
| **31 December 2009** | **7,006** | **182** | **105** | **296** | **7,589** |
| Total comprehensive income | | | | | |
| Profit for the year | - | - | - | 3 | **3** |
| Transactions with shareholders, recorded directly in equity | | | | | |
| Share capital increase | 1,000 | - | - | - | **1,000** |
| **31 December 2010** | **8,006** | **182** | **105** | **299** | **8,592** |
| Total comprehensive income | | | | | |
| Profit for the year | - | - | - | 453 | **453** |
| **31 December 2011** | **8,006** | **182** | **105** | **752** | **9,045** |

The accompanying notes on pages 13 to 65 form an integral part of these Bank's separate and consolidated financial statements.

The Bank's separate and consolidated financial statements as set out on pages 8 to 65 were authorised for issue by Board and Council on 27 March 2012.

D. Kalantirskijs
Chairman of the Council

S. Dzene
Chairperson of the Board

## BANK'S SEPARATE AND CONSOLIDATED STATEMENT OF CASH FLOW

| | | 2011 | 2011 | 2010 | 2010 |
|---|---|---|---|---|---|
| | | Group | Bank | Group | Bank |
| **Cash flows from operating activities** | Note | LVL '000 | LVL '000 | LVL '000 | LVL '000 |
| Profit (loss) before corporate income tax | | 542 | 539 | 76 | 3 |
| Depreciation | | 230 | 224 | 241 | 241 |
| Increase of impairment allowance | | 927 | 927 | 665 | 665 |
| Depreciation of investment property | | 24 | - | 27 | - |
| **Increase in cash and cash equivalents from operating activities before changes in assets and liabilities** | | **1,723** | **1,690** | **1,009** | **909** |
| Due from credit institutions (term over 3 months) | | (1,398) | (1,398) | (1,591) | (1,591) |
| Loans | | (10,369) | (12,506) | (12,528) | (12,840) |
| Shares and other non-fixed income securities | | (15) | (15) | (7) | (7) |
| Latvian government bonds with fixed income | | (395) | (395) | (2,116) | (2,116) |
| Fixed income debt securities | | (2,553) | (2,553) | - | - |
| (Increase)/decrease in deferred expenses and accrued income | | 17 | 11 | (4) | 2 |
| (Increase)/ decrease in other assets | | 184 | 203 | (153) | (255) |
| (Increase)/ decrease in assets held for sale | | (373) | - | - | - |
| Customers' deposits | | 28,765 | 28,723 | 35,717 | 35,766 |
| Increase/(decrease) in deferred income and accrued expense | | 90 | 65 | 2 | (1) |
| (Decrease)/increase in other liabilities | | (6,974) | (7,036) | 4,865 | 4,810 |
| Increase / (decrease) in provisions | | 5 | 4 | - | - |
| **Increase in cash and cash equivalents from operating activities before corporate income tax** | | **8,707** | **6,793** | **25,194** | **24,677** |
| Corporate income tax | | - | - | - | - |
| **Increase in cash and cash equivalents from operating activities after corporate income tax** | | **8,707** | **6,793** | **25,194** | **24,677** |
| **Cash flow from investing activities** | | | | | |
| Acquisition of property and equipment | | (252) | (178) | (237) | (237) |
| Purchase of investment property | | (1,840) | - | (517) | - |
| Profit from sale of items of property and equipment | | - | - | - | - |
| **Net cash flow from investing activities** | | **(2,092)** | **(178)** | **(754)** | **(237)** |
| **Cash flows from financing activities** | | | | | |
| Share issue | | - | - | 1,000 | 1,000 |
| Acquisition of subordinated loans | | 1,779 | 1,779 | 1,000 | 1,000 |
| **Increase in cash and cash equivalents from financing activities** | | **1,779** | **1,779** | **2,000** | **2,000** |
| **Net increase in cash and cash equivalents** | | **8,394** | **8,394** | **26,440** | **26,440** |
| **Cash and cash equivalents at the beginning of the year** | | **52,060** | **52,060** | **25,620** | **25,620** |
| **Cash and cash equivalents at the end of the year** | 29 | **60,454** | **60,454** | **52,060** | **52,060** |

The accompanying notes on pages 13 to 65 form an integral part of these Bank's separate and consolidated financial statements.

The Bank's separate and consolidated financial statements as set out on pages 8 to 65 were authorised for issue by Board and Council on 27 March 2012.

D. Kalantirskijs
Chairman of the Council

S. Dzene
Chairperson of the Board

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

### 1 GENERAL INFORMATION

**Information on the Bank**

AS "SMP Bank" (until 17 June 2008 AS "Multibanka" – the Bank) was incorporated in the Republic of Latvia as a joint stock company "Multibanka" in 1994, in Riga and is licensed as a bank offering a wide range of financial services to enterprises and individuals. The legal address of the Bank is Elizabetes iela 57, Riga, Latvia. The Bank has a branch in Liepaja and 16 cash offices in Riga, 3 cash offices in Daugavpils, 2 cash offices in Ventspils and cash offices in Olaine, Jelgava, Sigulda, Jurmala, foreign branch in Vilnius (Lithuania), with sub-branches in Klaipeda and Kaunas, and representative offices in Moscow and Yekaterinburg (Russia) and Kiev (Ukraine). In 2011 the Bank opened a branch in Vilnius, commencing operations in the Lithuanian market.

The consolidated and separate financial statements for year ended on 31 December 2011 include financial statements of the Bank and its controlled entity AS "SMP Finance" (hereinafter "Group"). The legal address of the AS "SMP Finance" is Elizabetes iela 57, Riga, Latvia.

**Legislation regulating the Bank's operations**

The Bank's operations are governed by the law of the Republic of Latvia "On Credit Institutions", "Commercial Law", and other laws and regulations issued by the Financial and Capital Market Commission ('FKTK'). The above regulations govern capital adequacy, minimum equity, liquidity, foreign exchange positions, risk transaction restrictions with respect to one counterparty, group of related customers and related parties of the Bank, as well as other applicable requirements.

### 2 BASIS OF PREPARATION

**Statement of compliance**

The consolidated and separate financial statements of the Group and the Bank are prepared in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union, and regulations of the Financial and Capital Market Commission in force as at 31 December 2011.

The Board and Council of the Bank approved these consolidated and separate financial statements for issue on 27 March 2012. The shareholders have the power to reject the consolidated and separate financial statements prepared and issued by the management, and the right to request that new financial statements be issued.

**Basis of measurement**

The financial statements are prepared on the historical cost basis except for the following:

- financial assets and liabilities at fair value through profit or loss are stated at fair value (including financial assets held for trading);
- all derivatives are carried at fair value;
- available-for-sale assets are stated at fair value except those whose fair value cannot be reliably estimated.

**Functional and Presentation Currency**

The accompanying financial statements are presented in thousands of Lats (LVL 000's), unless otherwise stated. Lats are the Bank's functional currency.

### 3 SIGNIFICANT ACCOUNTING POLICIES

The following significant accounting policies have been applied in the preparation of the financial statements. The following accounting policies have been consistently applied.

**Basis for consolidation**

*Subsidiaries*

For the purposes of the Group consolidated financial statements, subsidiaries are those enterprises controlled by the Bank. Control exists when the Bank has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control effectively commences until the date that control effectively ceases.

Intra-group transactions, balances and unrealized profits arising from intra-group transactions are eliminated in the course of consolidation.

The investment in AS "SMP Finance", in which the Bank holds a 48.73% interest and voting rights, is accounted for in the Bank's separate financial statements at cost less impairment.

On 11 May 2009 the Bank disposed of 50.97% or 316 shares of its investment in AS "SMP Finance" to two Board members and a council member of the Bank. The shares were disposed of at the nominal value, i.e. the total value of disposed shares was LVL 15 800. The Bank still retains control over AS "SMP Finance" through its management board, and therefore that company is included in consolidation.

*Foreign currency translation*

Transactions in foreign currencies are translated into the respective functional currency of the operations at the exchange rate set by Central banks at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated into the functional currency at the spot exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the period. Non-monetary assets and liabilities denominated in foreign currencies that are measured at cost or are measured at fair value are retranslated into the functional currency at the spot exchange rate at the date that the cost or fair value was determined, respectively. Foreign currency differences arising on retranslation are recognized in statement of comprehensive income, except for differences arising on the retranslation of available-for-sale equity instruments or a financial liability designated as the hedging instrument in a hedge of the net investment in a foreign operation or in a qualifying cash flow hedge, which are recognized directly in other comprehensive income. Non-monetary items that measured in terms of historical cost in foreign currency are translated using the exchange rate at the date of transaction.

The assets and liabilities of foreign operations are translated to the presentation currency at the exchange rate at reporting date. The income and expenses of foreign operations are translated to presentation currency at exchange rates that approximates those on the date of the transactions. Difference arising on translation to presentation currency are recognized in other comprehensive income.

Foreign exchange rates for the key currencies at the end of the reporting period were the following (LVL vs 1 unit of foreign currency):

| Currency | Reporting date | |
|---|---|---|
| | 31.12.2011 | 31.12.2010 |
| USD | 0.5440 | 0.5350 |
| EUR | 0.7028 | 0.7028 |
| LTL | 0.2040 | 0.2030 |
| RUB | 0.0170 | 0.0176 |

**Financial Instruments**

*Classification*

Financial instruments are classified into the following categories:

*Financial instruments at fair value through profit or loss* are financial assets or liabilities that are acquired or incurred principally for the purpose of selling or repurchasing in the near term; or that are part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking; or that are a derivative (except for a derivative that is a designated and effective hedging instrument); or that are upon initial recognition, designated by the entity as assets or liabilities measured at fair value through the profit or loss.

*Held-to-maturity assets* are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Group or the Bank has the positive intention and ability to hold to maturity, and which are not classified as measured at fair value through profit or loss, or available for sale or loans and receivables.

*Available-for-sale assets* are those financial assets that are designated as available-for-sale after the initial recognition or are not classified as loans and receivables, held-to-maturity investments or financial instruments at fair value through profit or loss.

*Loans and receivables* are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than (a) those that the Group and the Bank intend to sell immediately or in the short-term, (b) those that the Group and the Bank upon initial recognition classify as measured at the fair value through profit or loss or as available for sale; or (c) those for which the holder may not recover substantially all of its initial investments, other than because of credit deterioration. Loans and receivables include amounts due from credit institutions on term, loans and receivables from customers and other financial assets which comply to these classification criteria.

*Liabilities at amortised cost* include deposits and balances with the Bank of Latvia, deposits and balances from banks and current accounts and deposits from customers.

All regular way purchases and sales of investment securities are recognized at the settlement date, which is the date that an asset is delivered to or by an enterprise.

*Recognition*

The Group and the Bank initially recognises loans and receivables, deposits and debt securities issued on the date at which they are originated. All other financial assets and liabilities are recognised in the statement of financial position on the trade date when the Group or the Bank become a party to the contractual provisions of the instrument.

*Measurement*

A financial asset or liability is initially measured at its fair value plus, in the case of a financial asset or liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or liability.

Subsequent to initial recognition, financial assets, are measured at their fair values, without any deduction for transaction costs that may be incurred on sale or other disposal, except for:

- held-to-maturity investments and loans and receivables that are measured at amortized cost using the effective interest method; and
- investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are carried at cost.

All financial liabilities, other than those designated at fair value through profit or loss and financial liabilities that arise when a transfer of a financial asset carried at fair value does not qualify for derecognition, are measured at amortized cost. Amortised cost is calculated using the effective interest method. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortized based on the effective interest rate of the instrument. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability. When calculating the effective interest rate, the Group and the Bank estimates future cash flows considering all contractual terms of the financial instruments, but not future credit losses.

*Fair value basis*

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date.

When available, the Group and the Bank measure the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active, the Group and the Bank establishes fair value using a valuation technique. Valuation techniques include recent arm's length transactions between knowledgeable, willing parties (if available), reference to the current fair value of other instruments that are substantially the same, discounted cash flow analyses and option pricing models. The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates specific to the Group and the Bank, incorporates all factors that market participants would consider in setting a price, and is consistent with accepted economic methodologies for pricing financial instruments. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument. The Bank calibrates valuation techniques and tests them for validity using prices from observable current market transactions in the same instrument or based on other available observable market data.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price, i.e., the fair value of the consideration given or received, unless the fair value of that instrument is evidenced by information about other observable current market transactions with the same instrument (i.e., without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When transaction price provides the best evidence of fair value at initial recognition, the financial instrument is initially measured at the transaction price and any difference between this price and the value initially obtained from a valuation model is subsequently recognised in profit or loss depending on the individual facts and circumstances of the transaction but not later than when the valuation is supported by observable market data or the transaction is closed out.

Assets and long positions are measured at a bid price; liabilities and short positions are measured at an asking price. Where the Group and the Bank have positions with offsetting risks, mid-market prices are used to measure the offsetting risk positions and a bid or asking price adjustment is applied only to the net open position as appropriate. Fair values reflect the credit risk of the instrument and include adjustments to take account of the credit. Fair value estimates obtained from models are adjusted for any other factors, such as liquidity risk or model uncertainties, to the extent that the Bank believes a third-party market participant would take them into account in pricing a transaction.

*Gains and losses on subsequent measurement*

A gain or loss arising from a change in the fair value of a financial asset or liability is recognised as follows:

- a gain or loss on a financial instrument classified as at fair value through profit or loss is recognised in the statement of comprehensive income;
- a gain or loss on an available-for-sale financial asset is recognized directly in other comprehensive income (except for impairment losses and foreign exchange gains and losses) until the asset is derecognized, at which time the cumulative gain or loss previously recognized in equity is recognized in the statement of comprehensive income. Interest in relation to an available-for-sale financial asset is recognized as earned in the statement of comprehensive income calculated using the effective interest method. Interest in relation to an available-for-sale financial asset is recognized as earned in the statement of comprehensive income calculated using the effective interest method.

For financial assets and liabilities carried at amortised cost, a gain or loss is recognised in the statement of comprehensive income when the financial asset or liability is derecognised or impaired..

*Derecognition*

A financial asset is derecognised when the contractual rights to the cash flows from the financial asset expire or when the Group and the Bank transfer substantially all of the risks and rewards of ownership of the financial asset. Any rights or obligations created or retained in the transfer are recognised separately as assets or liabilities. A financial liability is derecognized when it is extinguished.

The Group and the Bank also derecognize certain assets when they write off balances pertaining to the assets deemed to be uncollectible.

*Offsetting*

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to set off the recognised amounts and the Bank has an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

*Repurchase and reverse repurchase agreements*

Securities sold under sale and repurchase ("repo") agreements are accounted for as secured financing transactions, with the securities retained in the statement of financial position and the counterparty liability included in amounts payable under repo transactions. The difference between the sale and repurchase price represents the interest expense and is recognised in the statement of comprehensive income over the term of the repo agreement using the effective interest rate method.

Securities purchased under agreements to resell ("reverse repo") are recorded as amounts receivable under reverse repo transactions. The differences between the purchase and resale prices are treated as interest income and accrued over the term of the reverse repo agreement using the effective interest method.

If assets purchased under agreement to resell are sold to third parties, the obligation to return securities is recorded as a trading liability and measured at fair value.

*Derivatives*

Derivative financial instruments including foreign exchange contracts, currency and interest rate swaps and other derivative financial instruments are initially recognized in the balance sheet at their fair value. Attributable transaction costs are recognized in the statement of comprehensive income when incurred. Fair values are obtained from quoted market prices and discounted cash flow models as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when the fair value is negative.

The Group and the Bank do not use hedge accounting.

*Interest-bearing liabilities*

Interest-bearing liabilities are initially recognized at fair value less any transaction costs incurred. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the statement of comprehensive income over the period of the borrowings, using effective interest method.. When borrowings are repurchased or settled before maturity, any difference between the amount repaid and the carrying amount is recognized immediately in the profit and loss in the statement of comprehensive income.

**Property and equipment**

*Owned assets*

Items of property and equipment are measured at cost less accumulated depreciation and impairment losses.

Where an item of property, plant and equipment comprises major components having different useful lives, they are accounted for as separate items of property, plant and equipment. Cost includes expenditures that is directly attributable to the acquisition of the asset.

*Depreciation*

Depreciation is charged to the statement of comprehensive income on a straight-line basis over the estimated useful lives of the individual assets. Depreciation commences on the date when available for use or, in respect of internally constructed assets, from the time an asset is completed and ready for use. Depreciation methods, useful lives and residual values are assessed annually. The annual depreciation rates are as follows:

| | |
|---|---|
| Buildings | 5% |
| Furniture and cars | 20% |
| Computers | 35% |
| Other items of property and equipment | 20% |

**Intangible assets**

Intangible assets, which are acquired by the Group or the Bank, are stated at cost less accumulated amortization and impairment losses.

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. Depreciation is charged to the statement of comprehensive income on a straight-line basis over the estimated useful lives of the individual assets. The estimated useful lives are 5 to 7 years.

**Investment property**

Investment property is property held either to earn rental income or for capital appreciation or for both, but not for sale in the ordinary course of business or services or for administrative purposes. Investment property is carried at cost less accumulated depreciation and impairment. Impairment is recognised in the statement of comprehensive income on a straight line basis. Annual depreciation rate of all investment properties, except land, is 5%. No depreciation is calculated for land.

**Repossessed assets**

As part of the normal course of business the Group and the Bank occasionally take possession of property that originally was pledged as security for a loan. When the Group and the Bank acquires (i.e. gains a full title to) a property in this way, the property's classification follows the nature of its intended use by the Group and Bank. When the Group and the Bank is uncertain of its intentions with respect to property that it has repossessed, those properties are classified as investment property. Other types of collateral (repossessed finance lease objects) are classified as other assets.

**Assets held for sale**

Non-current assets that are expected to be recovered primarily through sale or distribution rather than through continuing use, are classified as held for sale. Immediately before classification as held for sale, the assets or components of a disposal group, are remeasured in accordance with Group's accounting policies. Thereafter generally the assets, or disposal group, are measured at lower of their carrying amount and fair value less cost to sell. Any impairment loss on a disposal group is allocated first to goodwill, and then to the remaining assets and liabilities on pro rata basis, except that no loss is allocated to financial assets, deferred tax assets, employee benefit assets, investment property, which continue to be measured in accordance with the Group's accounting policies. Impairment losses on initial classification as held for sale and subsequent gains and losses on remeasurement are recognised in statement of comprehensive income. Gains are not recognised in excess of any cumulative impairment loss.

Once classified as held for sale, intangible assets and property, plant and equipment are no longer amortised and depreciated, and any equity-accounted investee is no longer equity accounted.

**Income and expense recognition**

All significant income and expense categories are recognized on an accrual basis.

Interest income and expense are recognized in the statement of comprehensive income as they accrue, taking into account the effective interest rate of the asset/liability. Interest income and expense include the amortization of any discount or premium or other differences between the initial carrying amount of an interest bearing instrument and its amount at maturity calculated on an effective interest rate basis.

Loan issuance fees and other fees together with the related direct costs that are considered integral part of the total loan profitability are deferred and amortised to the interest income over the estimated life of the financial instrument using the effective interest rate method.

Other fees, commissions and other income and expense items are recognised when the corresponding service has been provided.

**Impairment**

*Financial assets*

At each reporting date the Group and the Bank assess whether there is objective evidence that financial assets other than carried at fair value through profit or loss are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash flows of the asset that can be estimated reliably.

Objective evidence that financial assets (including equity securities) are impaired can include default or delinquency by a borrower, restructuring of a loan or advance by the Group and the Bank on terms that the Group and the Bank would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group. In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

The Group and the Bank consider evidence of impairment for loans and advances and held-to-maturity investment securities at specific asset level. All loans and advances and held-to-maturity investment securities are assessed for specific impairment.

Impairment losses on assets carried at amortized cost are measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognised in the profit and loss in the statement of comprehensive income and reflected in an allowance account against loans and receivables. Interest on the impaired asset continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss in the statement of comprehensive income.

Impairment losses on available-for-sale assets are recognised by transferring the cumulative loss that has been recognised directly in equity to profit or loss. The cumulative loss that is removed from equity and recognized in the profit and loss in the statement of comprehensive income is the difference between the acquisition cost, net of any principal repayment and amortization, and the current fair value, less any impairment loss previously recognized in the statement of comprehensive income . Changes in the impairment allowance attributable to time value are reflected as a component of interest income.

If, in a subsequent period, the fair value of an impaired available-for-sale bond increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the statement of comprehensive income, the impairment loss is reversed, with the amount of the reversal recognised in the statement of comprehensive income. Subsequent recovery in the fair value of impaired available-for-sale equity securities recognized in previous periods is recognized in the statement of comprehensive income.

*Non-financial assets*

The carrying amounts of the Group's and the Bank's non-financial assets, other than deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated.

An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets and groups. Impairment losses are recognised in profit or loss of the statement of comprehensive income of the current year. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

**Credit related commitments**

In the normal course of business, the Group and the Bank enters into credit related commitments, comprising undrawn loan commitments, letters of credit and guarantees, and provides other forms of credit insurance.

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

A financial guarantee liability is recognized initially at fair value net of associated transaction costs, and is measured subsequently at the higher of the amount initially recognized less cumulative amortization or the amount of provision for losses under the guarantee. Provisions for losses under financial guarantees and other credit related commitments are recognised when losses are considered probable and can be measured reliably.

Financial guarantee liabilities and provisions for other credit related commitments are included within other liabilities.

**Calculation of recoverable amount**

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

**Taxes**

Corporate income tax comprises current and deferred tax. Income tax expense is recognized in the statement of comprehensive income except to the extent that it relates to items recognized directly in equity or in other comprehensive income.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided on all temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss, and differences relating to investments in subsidiaries to the extent that they probably will not reverse in the foreseeable future. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

**Cash and cash equivalents**

Cash and cash equivalents comprise cash on hand, unrestricted deposits with the Bank of Latvia and high liquidity assets with a maturity of less than 3 months subject to insignificant changes in the fair value used by the Group and the Bank for covering short term liabilities; less balances due to the Bank of Latvia and credit institutions with original maturity of less than 3 months.

**Leases**

*Finance lease*

A finance lease is a lease that transfers substantially all the risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred.

When assets are leased out under a finance lease, the net investment in finance lease is recognized as a receivable. The net investment in finance lease represents the difference between the gross receivable and the unearned finance income.

*Operating lease*

An operating lease is a lease other than a finance lease.

Assets leased out under an operating lease, are presented within property and equipment in the statement of financial position, less accumulated depreciation. They are depreciated over their expected useful lives on a basis consistent with similar owned items of property and equipment.

**Provisions**

A provision is recognised in the statement of financial position when the Group and the Bank has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits that can be reliably estimated will be required to settle the obligation.

**Dividends**

The Group or the Bank receives dividends from the equity instruments that are recorded to income when the right to receive payment is established.

Proposed dividends are recognised in the financial statements only when approved by shareholders.

**Employee benefits**

Short term employee benefits, including salaries and social security contributions, bonuses and vacation benefits are included in net operating expenses on an accrual basis. The Group and the Bank pay fixed security contributions to the State Social Fund on behalf of its employees during the employment period in accordance with local legal requirements and the Group and the Bank will have no obligations to pay further contributions relating to employee services in respect to pension of retired employees.

## *Adoption of new and/or changed IFRSs and IFRIC interpretations*

*New Standards and Interpretations*

*New and amended standards and interpretations that became effective during the accounting period but are not applicable to the Group and Bank:*

- An amendment to standard IFRS 7 Disclosures related to the transfers of financial assets is effective for annual periods beginning after 1 July 2011, and this amendment has no significant impact on the financial statements of the Group and Bank.
- Revised IAS 24 Related Party Disclosures (effective for annual periods beginning on or after 1 January 2011). The amendment exempts a government-related entity from the disclosure requirements in relation to related party transactions and outstanding balances, including commitments, with (a) a government that has control, joint control or significant influence over the reporting entity; and (b) another entity that is a related party because the same government has control, joint control or significant influence over both the reporting entity and the other entity. The revised Standard requires specific disclosures to be provided if a reporting entity takes advantage of this exemption. The revised Standard also amends the definition of a related party which resulted in new relations being included in the definition, such as, associates of the controlling shareholder and entities controlled, or jointly controlled, by key management personnel. Revised IAS 24 does not result in new relations requiring disclosure in the Group's and Bank's financial statements.
- Amendment to IFRIC 14 IAS 19 – *The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction* (effective for annual periods beginning on or after 1 January 2011). The amendment of IFRIC 14 addresses the accounting treatment for prepayments made when there is also a minimum funding requirements (MFR). Under the amendments, an entity is required to recognize certain prepayments as an asset on the basis that the entity has a future economic benefit from the prepayment in the form of reduced cash outflows in future years in which MFR payments would otherwise be required. The amendments to IFRIC 14 is not relevant to the Group's

and Bank's financial statements as the Bank does not have any defined benefit plans with minimum funding requirements.

- FRIC 19 *Extinguishing Financial Liabilities with Equity Instruments* (effective for annual periods beginning on or after 1 July 2010). The Interpretation clarifies that equity instruments issued to a creditor to extinguish all or part of a financial liability in a 'debt for equity swap' are consideration paid in accordance with IAS 39.41. The initial measurement of equity instruments issued to extinguish a financial liability is at the fair value of those equity instruments, unless that fair value cannot be reliably measured, in which case the equity instrument should be measured to reflect the fair value of the financial liability extinguished. The difference between the carrying amount of the financial liability (or part of the financial liability) extinguished and the initial measurement amount of equity instruments issued should be recognized in profit or loss. The Group and Bank did not issue equity to extinguish any financial liability during the current period. Therefore, the Interpretation will have no impact on the comparative amounts in the Group's and Bank's financial statements for the year ended 31 December 2010. Since the Interpretation can relate only to transactions that will occur in the future, it is not possible to determine in advance the effects the application of the Interpretation will have.
- Amendment to IAS 32 *Financial Instruments: Presentation – Classification of Rights Issues* (effective for annual periods beginning on or after 1 February 2010). The amendment requires that rights, options or warrants to acquire a fixed number of the entity's own equity instruments for a fixed amount of any currency are equity instruments if the entity offers the rights, options or warrants pro rata to all of its existing owners of the same class of its own non-derivative equity instruments. The amendments to IAS 32 are not relevant to the Group's and Bank's financial statements as the Group and Bank have not issued such instruments at any time in the past.

## 4 RISK MANAGEMENT

Management of the Group and the Bank has developed a system for the identification, supervision and management of the Group's and the Bank's main financial risks. The Bank's management has approved risk management system. This system is being constantly updated to take into account market conditions and the development of the Group and the Bank's main operations. In order to achieve the Group's and the Bank's goals regarding capital adequacy, liquidity, foreign currency position and in order to control transaction risks, the following policies have been approved:

1. Liquidity risk management policy;
2. Credit risk management policy;
3. Risk transactions and risk control policy for large transactions;
4. Currency risk management policy;
5. Country risk management policy;
6. Interest rate risk management policy;
7. Policy on prevention of laundering of proceeds derived from criminal activity and terrorist financing;
8. Operational compliance risk management policy;
9. Capital adequacy assessment policy;
10. Operational risk management policy.

The Group and the Bank maintain adequate amounts of liquid assets to ensure compliance with required liquidity ratio of 30% against the Group and Bank's current liabilities as at 31 December 2011 and 31 December 2010. For this purpose, the Group and the Bank have approved internal limits of net items of assets and liabilities ageing structure liquidity: in all the currencies LVL, EUR and USD. Internal limits for liquidity are used for risk analysis and control of liquidity and desirable structure of financing sources. An early warning system was developed in order to help identify exposure of the Bank's liquidity position and necessity to attract additional sources. On basis of data from early notification indices the Bank identifies negative tendencies impacting liquidity and analyses the tendencies and assess necessity to perform liquidity risk hedging measures. The Risk and resource management department of the Bank evaluates and plans the term structure of assets and liabilities on a regular basis, and accordingly prepares timely plans for attraction or sales of financial resources, as well as monitors compliance with the required liquidity norms and internal limits defined by the Group and the Bank. Liquidity stress testing is performed using 6 scenarios. These scenarios address both internal and external factors. Stress testing is performed on the following stress levels: internal and typical to the Bank unfavourable events, changes of general market conditions, banking crisis and general market crisis at the same time. The impact of various scenarios on the regulating liquidity ratio and the Bank's income is analysed. The Board of the Bank develops and the Council approves a contingency plan in case of liquidity crisis that specifies: preventive measures for reduction of the likelihood of the liquidity crisis, methods of timely identification of the liquidity crisis and risk assessment, measures that have to be taken immediately in order to overcome the liquidity crisis.

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

In order to meet the requirements defined in the policy of management of large risk transactions, the Group and the Bank perform an assessment and control of risks associated with all assets and liabilities, including contingent liabilities of the Group and Bank on a regular basis. Limits are regarded as the main tool for the control of risk transactions. The assessment of credit risks enables the Group and the Bank to meet the required capital adequacy ratio – the proportion of weighted values of the Group and Bank's equity, assets, liabilities and off-balance items, which as at 31 December 2011 and 2010 was 11% and 11%, respectively. The Credit Institution Law and regulations developed by the Financial and Capital Market Commission for application of the norms of this law, require Latvian banks to maintain a capital adequacy ratio of 8%, i.e., Bank's capital ratio against the risk weighted assets and contingent liabilities and the sum of notional risk weighted assets and contingent liabilities. The sum of notional risk weighted assets and contingent liabilities is determined as the sum of capital requirements of market risks multiplied by 12.5. The requested capital adequacy ratio for the Bank is adjusted to 11% according to Financial and Capital Market Commission requirements effective 1 April 2012.

The assets have been weighted in accordance with pre-defined risk grades, determining risks in accordance with the amount of capital, necessary to maintain these assets. Off-balance sheet loan liabilities are weighted in accordance with lending risk adjustment grades and risk grades defined for liabilities of partners. The following risk grades are applied: 0%, 20%, 35%, 50%, 100%, 150%.

The Bank's objectives when managing capital, which is a broader concept than the "equity" on the face of the statement of financial position, are:

- To comply with the capital regulatory requirements,
- To safeguard the Bank's ability to continue as a going concern so that it can continue providing returns for shareholders,
- To maintain a strong capital base to support the development of its business.

Capital adequacy and the use of regulatory capital are monitored daily by the Bank's management, employing techniques based on the guidelines developed by the Basel Committee and the European Union directives, as implemented by the Financial and Capital Market Commission. The required information is filed with the Financial and Capital Market Commission on a monthly basis.

The guidelines of the Financial and Capital Market Commission for calculation of capital adequacy basically agree to the recommendations under the Basle Capital Accord and amendments thereto. According to the Basle Capital Accord, the capital adequacy ratio should be at least 8%. For the calculation of capital adequacy refer to Note 36.

During 2011, the Group and the Bank performed daily controls of compliance with limits defined in Currency risk management policy, for transactions with foreign currency. The Group and the Bank are subject to the Credit Institutions Law which requires that the open position in an individual currency should not exceed 10% of the Bank's capital and the total open foreign currency position should not exceed 20% of the Bank's capital. In accordance with requirements of Currency risk management policy, structural units of the Group and the Bank are cooperating with department of financial operations in evaluation of currency risk component of the planned transactions and elaboration of hedging method for it.

An analysis of sensitivity of the Group's and the Bank's net income for the year and equity to changes in the foreign currency exchange rates based on positions existing as at 31 December 2010 and 2011 and a simplified scenario of a 10% change in USD or EUR to LVL exchange rates is as follows:

**Group**

| | 2011 | 2010 |
|---|---|---|
| **'000 LVL** | **Net profit** | **Net profit** |
| 10% appreciation of USD against LVL | (32) | (8) |
| 10% depreciation of USD against LVL | 32 | 8 |
| 10% appreciation of EUR against LVL | (10) | 4 |
| 10% depreciation of EUR against LVL | 10 | (4) |

**Bank**

| | 2011 | 2010 |
|---|---|---|
| **'000 LVL** | **Net profit** | **Net profit** |
| 10% appreciation of USD against LVL | (1) | 4 |
| 10% depreciation of USD against LVL | 1 | (4) |
| 10% appreciation of EUR against LVL | 51 | 49 |
| 10% depreciation of EUR against LVL | (51) | (4) |

The foreign exchange rate of LVL is pegged to EUR as at 31 December 2011 and 31 December 2010.

Interest risk is represented by possible negative influence on the Group and the Bank's income that can result from possible changes of interest rates. The GAP analysis is used for daily measurements of interest rates risk. Assets, liabilities, guarantees and contingent liabilities, subjected to interest rate risk, are divided in accordance with minimum period, left till possible re-evaluation of interest rates. The Group and the Bank calculate the influence on yearly net interest income, with parallel increase of interest rates for 100 base points. In accordance with requirements of Interest rate risk management policy, the respective component of interest rate risk is assessed when limits are determined for any financial tool. For the sensitivity analysis results refer to Note 33.

Country risk is represented by possible losses in cases, where a debtor of the Group and the Bank, being non-resident, will not be able to meet its liabilities against the Group and the Bank, due to political, social or economic circumstances of the country of residency of the debtor. Country risk is managed by the Board of the Bank. Based on analyses of economic, political and social conditions of each particular country, limits are determined for geographic concentration of assets, guarantees and contingent liabilities, for purpose of management of country risk. The evaluation of each case separately provided by international rating agencies is considered when assessing country risk in each separate case. Limitations have been approved for placement of assets in non-OECD countries, as well as for limitations on residual balances of nostro accounts. Limits for partners and transaction types are determined based on evaluation of risks of country and partners. For purpose of monitoring of compliance with these limits, control over observation of limits is performed on daily basis.

In order to avoid involvment in "money-laundering" schemes, the Group and the Bank have implemented policies and procedures to prevent AML and anti-terrorism financing. AML compliance risks may cause financial losses, arising from legal actions and eventual financial sanctions against the Group and the Bank, as well as from limitations on banking operations, loss of customers or its place on financial markets. The Group and the Bank manage their AML compliance risks on regular basis, identifying legal, reputational, operational and concentration risks, as well as planning and performing necessary measures to minimise those risks based on requirements of AML strategy and Customer policy that has been developed and approved by the Group and the Bank. These requirements are based on the adequate identification of a customer and its beneficial owner and "Know Your Customer" principles of their business, as well as identification of unusual and suspicious transactions, its control and reporting to state authorities according to requirements of applicable legislative acts. AML compliance action plan includes also AML training of staff of structural units of the Group and the Bank, involved with servicing of customers and implementation of latest IT technologies and requirements of information security and data integrity principles in daily operations of the Group and the Bank.

Operational risk is the risk of loss resulting from inadequate or failed internal processes for the Group and the Bank, people and systems or from external events, including legal risk, but excluding strategic risk and reputation risks. Operational risk is related to the all types of products, activities, processes and systems, the Group and the Bank are dealing with. A primary objective of operational risk management is protection of the Group's and the Bank's assets and capital, by minimising eventual operational risk related losses and the frequency of the operational risk related cases. In line with the sound operational risk management process, the code of ethics is developed to be followed at all levels of the organizational structure of the Group and the Bank as well the effective internal control system has been set up. In order to identify and evaluate operational risk, the operational risk cases comprising database is developed in the Group and the Bank and operational risk self-estimation is carried out. A set of indicators, reflecting the possible sources for operational risk level increase, is elaborated to monitor operational risk. To minimise the operational risk, data handling procedures, along with the IT security technologies as well as insurance of assets are used. To ensure a continuous performance of the Group and the Bank, as well as to minimise the possible emergency cases related losses, the Board of the Bank specifies activity related critical functions, develops and improves the Group and the Bank information system overall contingency plan, vital information systems backup procedures and the related contingency plans.

Operational compliance risk is the risk that the Bank may incur losses or be subject to legal obligations or sanctions or the Bank's reputation may deteriorate if the Bank fails to comply with or breaches compliance laws, rules and standards. In order to perform control and management of operational compliance risk the Bank has established a separate structural unit ensuring that its functions are independent from the operations of the Bank's structural units that are controlled by it. The identification and assessment of operational compliance risk is performed through planned inspections and analysis of the statistic and analytic data of the Bank's operations. The results of such inspections and recommendations regarding the reduction of operational compliance risks are regularly provided to the Board of the Bank.

## 5 USE OF ESTIMATES AND JUDGMENTS

The preparation of financial statements in conformity with IFRSs as adopted by the EU requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgments about carrying values of assets and liabilities that are not readily apparent from other sources. Although such estimates are based on the best of management's knowledge, the actual results may differ from these estimates.

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

**Key sources of estimation uncertainty:**

*Impairment allowance for loans and receivables*

The specific component of the total allowances for impairment applies to financial assets evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgements about each counterparty's financial situation and the net realisable value of any underlying collateral. Each impaired asset is assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable are independently approved by the Credit Risk function.

*Valuation of financial instruments*

The determination of fair value for financial assets and liabilities for which there is no observable market price requires the use of valuation techniques as described in accounting policy. For financial instruments that trade infrequently and have little price transparency, fair value is less objective, and requires varying degrees of judgment depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument.

*Impairment of financial instruments (other than loans)*

The determination of impairment indication is based on comparison of the financial instrument's carrying amount and fair value. Due to downturns on financial and capital markets, the market price is not always a reliable source for impairment indication. The Group and the Bank uses valuation models based on quoted market prices of similar products.

For the purposes of impairment loss measurement, the Bank's management makes estimates of any expected changes in future cash flows from a specific financial instrument based on analysis of financial position of the issuer of the financial instrument.

*Deferred tax asset recognition*

A deferred tax asset is recognized to the extent that it is probable that taxable profits will be available against which the deductible temporary differences can be utilised.

*Classification of lease*

Only risks and rewards incidental to ownership of the leased asset during the lease period should be considered when determining lease classification. Relevant risks include the possibility of losses from idle capacity or technological obsolescence and from decreases in the value of the asset; relevant rewards may include the gain from the increase in value of the asset or realization of the residual value at the end of the lease. Conversely, risks associated with construction of the asset prior to lease commencement, financing such construction and the costs of providing services using the leased asset, are not incidental to ownership of the leased asset during the lease period and, in the Management's view generally should be disregarded in evaluating the classification of the lease. The classification of a lease is determined at the inception of the lease and is not revised unless the lease agreement is modified.

*Classification of noncurrent assets as held-for-sale*

Assets, including subsidiaries, are classified as non-current assets as held for sale if their carrying amounts will be recovered principally through a sale transaction. For this to be the case, the asset must be available for immediate sale in its present condition and its sale must be highly probable.

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

### Determining fair values of financial instruments

The table below analyses financial instruments measured at fair value at the end of reporting period, by the level in fair value hierarchy into which the fair value measurement is categorized:

### The Group and the Bank

| **2011** | **Level 1** |
|---|---|
| **Financial assets** | |
| Non-fixed income securities | 35 |
| | **35** |
| | |
| **2010** | |
| **Financial assets** | |
| Non-fixed income securities | 20 |
| | **20** |

Level 1: Included in this category are financial assets and liabilities that are measured in whole or in part by reference to published quotes in an active market. A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis. Main asset classes included in this category are financial assets for which the fair value is obtained via pricing vendors or binding broker quotes and assets for which the fair value is determined by reference to indices.

## 6 CASH AND DUE FROM THE BANK OF LATVIA

| | 2011 | 2011 | 2010 | 2010 |
|---|---|---|---|---|
| **LVL '000** | **Group** | **Bank** | **Group** | **Bank** |
| Cash | 3,014 | 3,014 | 1,935 | 1,935 |
| Due from the Bank of Latvia (including minimum reserve deposit) | 8,092 | 8,092 | 9,455 | 9,455 |
| **Total** | **11,106** | **11,106** | **11,390** | **11,390** |

Due from the Bank of Latvia represents the balance outstanding on correspondent account with the Bank of Latvia.

According to the regulations of the Bank of Latvia, the Bank is required to maintain obligatory reserves with the Bank of Latvia equal to 3% of the average monthly balances due to credit institutions with maturity of over 2 years and equal to 5% of average monthly balances of all other liabilities included in the base of this reserve (calculated based on ratios of four reporting dates within a month):

- Demand and term deposits (non credit institutions)
- Due to credit institutions (except the Bank of Latvia)- Bonds and other debt securities issued by the Bank.

The compulsory reserve is compared to the Bank's average monthly correspondent account balance in LVL. The Bank's average correspondent balance should exceed the compulsory reserve requirement.

## 7 DEMAND DEPOSITS WITH CREDIT INSTITUTIONS

| LVL '000 | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| Credit institutions registered in OECD countries | 23,763 | 23,763 | 45,369 | 45,369 |
| Latvian credit institutions | 11,573 | 11,573 | 191 | 191 |
| Credit institutions registered in non-OECD countries | 10,547 | 10,547 | 705 | 705 |
| | **45,883** | **45,883** | **46,265** | **46,265** |

The Bank maintained business relationships with 32 correspondent banks (2010: 33).

The main correspondent banks:

| | 2011 | 2010 |
|---|---|---|
| Raiffeisen Bank International AG – Wien, Austria | 8,322 | 40,732 |
| Nordea Bank Finland Plc Latvijas filiāle | 8,000 | - |

## 8 LATVIAN GOVERNMENT DEBT SECURITIES WITH FIXED INCOME

| | | 2011 | 2011 | 2010 | 2010 |
|---|---|---|---|---|---|
| | | **Group** | **Bank** | **Group** | **Bank** |
| | **Maturity** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** |
| Latvian government bonds with fixed income (S&P – BB, Moody's – Baa 3) | 2011 | - | - | 3,103 | 3,103 |
| | 2012 | 2,423 | 2,423 | - | - |
| | 2021 | 1,075 | 1,075 | - | - |
| | | **3,498** | **3,498** | **3,103** | **3,103** |

## 9 FIXED INCOME DEBT SECURITIES

| | Maturity | 2011 Group LVL '000 | 2011 Bank LVL '000 | 2010 Group LVL '000 | 2010 Bank LVL '000 |
|---|---|---|---|---|---|
| Promsvjzjabank, Russian Federation (S&P – B) | 2012 | 1,120 | 1,120 | - | - |
| Alfa Bank, Russian Federation (S&P – BB) | 2013 | 1,152 | 1,152 | - | - |
| Credit Bank of Moscow, Russian Federation (S&P – BB) | 2014 | 281 | 281 | - | - |
| | | **2,553** | **2,553** | - | - |

## 10 LOANS AND TERM DEPOSITS DUE FROM CREDIT INSTITUTIONS

| LVL '000 | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| Term deposits with credit institutions | 5,051 | 5,051 | 4,129 | 4,129 |
| Due from other credit institutions | 2,094 | 2,094 | 1,257 | 1,257 |
| **Total loans and term deposits** | **7,145** | **7,145** | **5,386** | **5,386** |

As at 31 December 2011 the Group and the Bank had due from credit institutions amounting to LVL 2,094 thousand (2010: LVL 1,257 thousand) that secured collaterals for the guarantees issued by the Bank.

*Geographic analysis:*

| LVL '000 | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| Residents of OECD countries | 2,094 | 2,094 | 2,862 | 2,862 |
| Residents of Latvia | - | - | 1,000 | 1,000 |
| Residents of non-OECD countries | 5,051 | 5,051 | 1,524 | 1,524 |
| **Total loans and term deposits** | **7,145** | **7,145** | **5,386** | **5,386** |

## 11 LOANS

(a) Loans by groups are comprised as follows:

| LVL '000 | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| Individuals | 20,223 | 16,560 | 20,747 | 18,084 |
| Legal entities | 52,589 | 59,956 | 41,654 | 45,884 |
| Bank employees | 461 | 461 | 503 | 503 |
| **Total loans, gross** | **73,273** | **76,977** | **62,904** | **64,471** |
| | | | | |
| Impairment allowance | (2,788) | (2,787) | (1,861) | (1,860) |
| **Total loans, net** | **70,485** | **74,190** | **61,043** | **62,611** |

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

(b) Analysis of loans by types:

| | 2011 | 2011 | 2010 | 2010 |
|---|---|---|---|---|
| **LVL '000** | **Group** | **Bank** | **Group** | **Bank** |
| Loans | 54,656 | 58,360 | 51,695 | 53,262 |
| Credit lines | 18,410 | 18,410 | 10,799 | 10,799 |
| Overdrafts | 207 | 207 | 410 | 410 |
| **Loans, gross** | **73,273** | **76,977** | **62,904** | **64,471** |
| Impairment allowance | (2,788) | (2,787) | (1,861) | (1,860) |
| **Total loans, net** | **70,485** | **74,190** | **61,043** | **62,611** |

(c) Loans issued by industry, gross:

| | 2011 | | 2011 | | 2010 | | 2010 | |
|---|---|---|---|---|---|---|---|---|
| **Legal entities** | **Group** | | **Bank** | | **Group** | | **Bank** | |
| Real estate | 9,526 | 18% | 9,526 | 16% | 12,781 | 31% | 12,781 | 28% |
| Construction | 6,051 | 12% | 6,051 | 10% | 5,605 | 13% | 5,605 | 12% |
| Electricity | 4,885 | 9% | 4,885 | 8% | 1,042 | 3% | 1,042 | 2% |
| Trade | 11,653 | 22% | 11,653 | 19% | 6,932 | 17% | 6,932 | 15% |
| Manufacturing | 8,287 | 16% | 8,287 | 14% | 7,796 | 19% | 7,796 | 17% |
| Transport, storage and communications | 3,155 | 6% | 3,155 | 5% | 3,150 | 7% | 3,150 | 7% |
| Loans issued to financial intermediaries | - | - | 11,652 | 19% | - | - | 6,353 | 14 |
| Mortgage lease | 3,783 | 8% | - | - | 1,920 | 5% | - | - |
| Other | 5,249 | 9% | 4,747 | 9% | 2,428 | 5% | 2,225 | 5% |
| **Total** | **52,589** | **100%** | **59,956** | **100%** | **41,654** | **100%** | **45,884** | **100%** |
| **Individuals and personnel of the Bank** | | | | | | | | |
| Consumer loans | 406 | 2% | 406 | 2% | 419 | 2% | 419 | 2% |
| Credit cards | 376 | 2% | 376 | 2% | 412 | 2% | 412 | 2% |
| Car loans | 6 | - | 4 | - | 9 | - | 6 | - |
| Mortgage loans | 8,827 | 43% | 8,827 | 53% | 9,736 | 46% | 9,736 | 53% |
| Mortgage lease | 4,123 | 20% | - | - | 2,654 | 12% | - | - |
| Loans for business | 5,880 | 28% | 5,880 | 34% | 6,268 | 29% | 6,268 | 34% |
| Other | 1,066 | 5% | 1,528 | 9% | 1,752 | 9% | 1,746 | 9% |
| **Total** | **20,684** | **100%** | **17,021** | **100%** | **21,250** | **100%** | **18,587** | **100%** |

(d) Loans by geographical classification:

| | 2011 | 2011 | 2010 | 2010 |
|---|---|---|---|---|
| **LVL '000** | **Group** | **Bank** | **Group** | **Bank** |
| Residents of Latvia | 64,611 | 68,315 | 59,114 | 60,681 |
| Residents of OECD countries | 4,634 | 4,634 | 2,800 | 2,800 |
| Residents of non-OECD countries | 4,028 | 4,028 | 990 | 990 |
| **Non-banking loans and receivables, gross** | **73,273** | **76,977** | **62,904** | **64,471** |
| Impairment allowance | (2,788) | (2,787) | (1,861) | (1,860) |
| **Loans and receivables, net:** | **70,485** | **74,190** | **61,043** | **62,611** |

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

(e) Movements in the impairment allowance

| LVL '000 | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| **Balance at the beginning of the year** | **1,861** | **1,860** | **1,196** | **1,195** |
| Increase in allowances | 1,131 | 1,131 | 755 | 755 |
| Recovery of prior period loan loss allowances | (204) | (204) | (90) | (90) |
| *Net impairment allowance expense changes* | *927* | *927* | *665* | *665* |
| **Balance at the end of the reporting period** | **2,788** | **2,787** | **1,861** | **1,860** |

(f) Loans and accrued interest depending on delay of payments:

### Group

| LVL '000 | | Loans without delayed payments | Loans for which the payments have not been made in the agreed period | | | | | |
|---|---|---|---|---|---|---|---|---|
| Loans | | | Up to 30 days | 30-60 days | 61-90 days | 91-180 days | 181-360 days | More than 360 days |
| **31 December 2011** | | | | | | | | |
| Loans, gross | **73,273** | 65,147 | 455 | 466 | 154 | 1,136 | 3,691 | 2,224 |
| Impairment allowance | **(2,788)** | (1,001) | (29) | (4) | (39) | (103) | (433) | (1,179) |
| **31 December 2010** | | | | | | | | |
| Loans, gross | **62,904** | 58,791 | 490 | 595 | 36 | 534 | 564 | 1,894 |
| Impairment allowance | **(1,861)** | (738) | (69) | (69) | (6) | (19) | (149) | (811) |

### Bank

| LVL '000 | | Loans without delayed payments | Loans for which the payments have not been made in the agreed period | | | | | |
|---|---|---|---|---|---|---|---|---|
| Loans | | | Up to 30 days | 30-60 days | 61-90 days | 91-180 days | 181-360 days | More than 360 days |
| **31 December 2011** | | | | | | | | |
| Loans, gross | **76,977** | 68,852 | 455 | 466 | 154 | 1,136 | 3,691 | 2,223 |
| Impairment allowance | **(2,787)** | (1,001) | (29) | (4) | (39) | (103) | (433) | (1,178) |
| **31 December 2010** | | | | | | | | |
| Loans, gross | **64,471** | 60,359 | 490 | 595 | 36 | 534 | 564 | 1,893 |
| Impairment allowance | **(1,860)** | (738) | (69) | (69) | (6) | (19) | (149) | (810) |

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

(h) Loan classification by collateral quality assessment:

The table below shows separate loan groups by their carrying amount. The Group and the Bank have secured the loans issued to individuals with mortgages, pledge on assets and guarantees. Loan quality by groups:

| | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| **Loans to legal entities secured with a collateral** | | | | |
| Loans without impairment allowances | 36,643 | 36,643 | 32,999 | 32,999 |
| *Loans without delayed payments* | *35,922* | *35,922* | *32,405* | *32,405* |
| *Payments delayed up to 90 days* | *276* | *276* | *279* | *279* |
| *Payments delayed more than 90 days* | *445* | *445* | *315* | *315* |
| Loans with impairment allowances | 6,956 | 6,956 | 3,726 | 3,726 |
| *Loans without delayed payments* | *3,560* | *3,560* | *3,131* | *3,131* |
| *Payments delayed up to 90 days* | - | - | - | - |
| *Payments delayed more than 90 days* | *3,396* | *3,396* | *595* | *595* |
| Impairment allowance | (1,088) | (1,088) | (641) | (641) |
| **Total loans issued to legal entities** | **42,511** | **42,511** | **36,084** | **36,084** |
| **Finance lease** | | | | |
| Lease without impairment allowances | 7,909 | 4 | 4,577 | 6 |
| *Lease without delayed payments* | *7,909* | *4* | *4,577* | *6* |
| *Payments delayed up to 90 days* | - | - | - | - |
| Lease with impairment allowances | 1 | - | 1 | - |
| *Lease without delayed payments* | - | - | - | - |
| *Delayed lease payments* | *1* | - | *1* | - |
| Impairment allowance | (1) | - | (1) | - |
| **Total finance lease** | **7,909** | **4** | **4,577** | **6** |
| **Mortgage loans** | | | | |
| Loans without impairment allowances | 6,125 | 6,125 | 7,163 | 7,163 |
| *Loans without delayed payments* | *5,193* | *5,193* | *6,555* | *6,555* |
| *Payments delayed up to 90 days* | *383* | *383* | *427* | *427* |
| *Payments delayed more than 90 days* | *549* | *549* | *181* | *181* |
| Loans with impairment allowances | 2,702 | 2,702 | 2,573 | 2,573 |
| *Loans without delayed payments* | *648* | *648* | *1,368* | *1,368* |
| *Payments delayed up to 90 days* | *226* | *226* | *304* | *304* |
| *Payments delayed more than 90 days* | *1,828* | *1,828* | *901* | *901* |
| Impairment allowance | (745) | (745) | (577) | (577) |
| **Total mortgage loans** | **8,082** | **8,082** | **9,159** | **9,159** |

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

| | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| **Loans to private individuals secured by other collateral** | | | | |
| Loans without impairment allowances | 5,554 | 5,554 | 7,175 | 7,175 |
| *Loans without delayed payments* | *5,324* | *5,324* | *7,154* | *7,154* |
| *Payments delayed up to 90 days* | *102* | *102* | *7* | *7* |
| *Payments delayed more than 90 days* | *128* | *128* | *14* | *14* |
| Loans with impairment allowances | 2,000 | 2,000 | 1,087 | 1,087 |
| *Loans without delayed payments* | *1,766* | *1,766* | *163* | *163* |
| *Payments delayed up to 90 days* | *41* | *41* | *46* | *46* |
| *Payments delayed more than 90 days* | *193* | *193* | *878* | *878* |
| Impairment allowance | (499) | (499) | (450) | (450) |
| **Total loans to individuals** | **7 ,055** | **7 ,055** | **7 ,812** | **7 ,812** |

The amounts shown in the table below represent the gross carrying value of the loans by type of collateral and do not necessarily represent the fair value of the underlying collateral.

| | 31 December 2011 | | | | 31 December 2010 | | | |
|---|---|---|---|---|---|---|---|---|
| | Group | | Bank | | Group | | Bank | |
| | LVL '000 | % | LVL '000 | % | LVL '000 | % | LVL '000 | % |
| Commercial buildings | 23,923 | 33% | 23,923 | 31% | 25,564 | 41% | 25,564 | 39% |
| Commercial assets pledge | 9,900 | 14% | 9,900 | 13% | 2,432 | 4% | 2,432 | 4% |
| Land mortgage | 5,835 | 8% | 5,835 | 7% | 6,000 | 9% | 6,000 | 9% |
| Mortgage on residential properties | 17,184 | 23% | 17,184 | 22% | 18,563 | 29% | 18,563 | 29% |
| Guarantee | 2,749 | 4% | 2,749 | 4% | 1,774 | 3% | 1,774 | 3% |
| Other | 8,262 | 11% | 394 | 1% | 4,968 | 8% | 396 | 1% |
| No collateral | 5,420 | 7% | 16,992 | 22% | 3,603 | 6% | 9,742 | 15% |
| **Total** | **73,273** | **100%** | **76,977** | **100%** | **62,904** | **100%** | **64,471** | **100%** |

### Significant credit risk concentration

As at 31 December 2011 and 31 December 2010, the Bank had 17 and 18 borrowers or groups of related borrowers, whose total loan liabilities exceeded 10% of the Bank's capital stated in note 37. Gross amount of the above loans as at 31 December 2011 and 31 December 2010 was LVL 17 108 thousand and LVL 24,286 thousand, respectively.

According to the regulating requirements, the Bank's credit risk exposure with one customer or a group of related customers must not exceed 25% of the Bank's capital. As at 31 December 2011, the Bank was in compliance with the aforementioned requirement.

(i) Impaired loans

### Group

| | 2011 '000 LVL | 2010 '000 LVL |
|---|---|---|
| Impaired loans, gross | 9,889 | 7,991 |
| Impairment allowance | (2,788) | (1,861) |
| **Loans and receivables, net:** | **7,101** | **6,130** |

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

**Bank**

| | 2011<br>'000 LVL | 2010<br>'000 LVL |
|---|---|---|
| Impaired loans, gross | 9,888 | 7,989 |
| Impairment allowance | (2,787) | (1,860) |
| **Loans and receivables, net:** | **7,101** | **6,129** |

When reviewing the loans the Group and the Bank set the following categories for individual loans to assess their credit risk:

**Group**

| 2011<br>'000 LVL | Gross | Impairment allowance |
|---|---|---|
| Standard | 61,252 | - |
| Watch | 9,263 | 1,200 |
| Substandard | 1,759 | 621 |
| Doubtful | 611 | 579 |
| Lost | 388 | 388 |
| **Total** | **73,273** | **2,788** |

| 2010<br>'000 LVL | Gross | Impairment allowance |
|---|---|---|
| Standard | 54,747 | - |
| Watch | 6,123 | 799 |
| Substandard | 1,301 | 394 |
| Doubtful | 229 | 164 |
| Lost | 504 | 504 |
| **Total** | **62,904** | **1,861** |

**Bank**

| 2011<br>'000 LVL | Gross | Impairment allowance |
|---|---|---|
| Standard | 64,957 | - |
| Watch | 9,263 | 1,200 |
| Substandard | 1,759 | 621 |
| Doubtful | 611 | 579 |
| Lost | 387 | 387 |
| **Total** | **76,977** | **2,787** |

| 2010<br>'000 LVL | Gross | Impairment allowance |
|---|---|---|
| Standard | 56,315 | - |
| Watch | 6,123 | 799 |
| Substandard | 1,301 | 394 |
| Doubtful | 229 | 164 |
| Lost | 503 | 503 |
| **Total** | **64,471** | **1,860** |

*Restructured loans*

During the twelve month period ended 31 December 2011, the Group and the Bank restructured loans in the total amount of:

| **LVL '000** | **31 December 2011 '000 LVL** | **31 December 2010 '000 LVL** |
|---|---|---|
| Postponed payments of the principal and interest | 7,101 | 2,268 |
| **Total** | **7,101** | **2,268** |

(j) Finance lease receivables

Loans and advances to customers include the following finance lease receivables for leases of certain items of property and equipment where the Group is lessor:

| **LVL '000** | **2011** | **2010** |
|---|---|---|
| Gross investment in finance lease, receivables with maturity: | | |
| Less than one year | 1,3791 | 250 |
| Between one and five years | 4,094 | 1,822 |
| More than 5 years | 3,598 | 3,357 |
| **Total gross investment in finance lease, receivables:** | **9,071** | **5,429** |
| Unearned interest income | (1,162) | (852) |
| **Net investment in finance lease** | **7,909** | **4,577** |
| | | |
| **Net investments in finance lease with maturity:** | | |
| Less than one year | 1,110 | 243 |
| Between one and five years | 3,455 | 1,627 |
| More than 5 years | 3,344 | 2,707 |
| | **7,909** | **4,577** |

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

## 12 PROPERTY AND EQUIPMENT

### Group property and equipment

| LVL '000 | Buildings | Vehicles | Office equipment | Long term leasehold improvements | Total |
|---|---|---|---|---|---|
| **Historical cost** | | | | | |
| **31 December 2009** | **380** | **46** | **708** | **116** | **1,250** |
| Additions | - | - | 237 | - | 237 |
| Disposed | - | - | (262) | - | (262) |
| **31 December 2010** | **380** | **46** | **683** | **116** | **1,225** |
| Additions | - | 74 | 178 | - | 252 |
| Disposed | - | - | (151) | - | (151) |
| **31 December 2011** | **380** | **120** | **710** | **116** | **1,326** |
| | | | | | |
| **Accumulated depreciation** | | | | | |
| **31 December 2009** | **44** | **30** | **398** | **53** | **525** |
| Charge for the year | 19 | 9 | 180 | 33 | 241 |
| Depreciation of disposed items of property and equipment | - | - | (262) | - | (262) |
| **31 December 2010** | **63** | **39** | **316** | **86** | **504** |
| Charge for the year | 19 | 13 | 175 | 23 | 230 |
| Depreciation of disposed items of property and equipment | - | - | (151) | - | (151) |
| **31 December 2011** | **82** | **52** | **340** | **109** | **583** |
| | | | | | |
| **Balance** | | | | | |
| **31 December 2009** | **336** | **16** | **310** | **63** | **725** |
| **31 December 2010** | **317** | **7** | **367** | **30** | **721** |
| **31 December 2011** | **298** | **68** | **370** | **7** | **743** |

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

### Bank property and equipment

| LVL '000 | Buildings | Vehicles | Office equipment | Long term leasehold improvements | Total |
|---|---|---|---|---|---|
| **Historical cost** | | | | | |
| **31 December 2009** | **380** | **46** | **708** | **116** | **1,250** |
| Additions | - | - | 237 | - | 237 |
| Disposed | - | - | (262) | - | (262) |
| **31 December 2010** | **380** | **46** | **683** | **116** | **1,225** |
| Additions | - | - | 178 | - | 178 |
| Disposed | - | - | (151) | - | (151) |
| **31 December 2011** | **380** | **46** | **710** | **116** | **1,252** |
| | | | | | |
| **Accumulated depreciation** | | | | | |
| **31 December 2009** | **44** | **30** | **398** | **53** | **525** |
| Charge for the year | 19 | 9 | 180 | 33 | 241 |
| Depreciation of disposed items of property and equipment | - | - | (262) | - | (262) |
| **31 December 2010** | **63** | **39** | **316** | **86** | **504** |
| Charge for the year | 19 | 7 | 175 | 23 | 224 |
| Depreciation of disposed items of property and equipment | - | - | (151) | - | (151) |
| **31 December 2011** | **82** | **46** | **340** | **109** | **577** |
| | | | | | |
| **Balance** | | | | | |
| **31 December 2009** | **336** | **16** | **310** | **63** | **725** |
| **31 December 2010** | **317** | **7** | **367** | **30** | **721** |
| **31 December 2011** | **298** | **-** | **370** | **7** | **675** |

## 13 INVESTMENT PROPERTY

Investment property of the Group.

| | Land | Buildings | Total |
|---|---|---|---|
| **Historical cost** | | | |
| **31 December 2009** | **341** | **691** | **1,032** |
| Acquisitions | 517 | - | 517 |
| **31 December 2010** | **858** | **691** | **1,549** |
| Acquisitions | - | 1,840 | 1,840 |
| **31 December 2011** | **858** | **2,531** | **3,389** |
| | | | |
| **Accumulated depreciation** | | | |
| **31 December 2009** | **-** | **7** | **7** |
| Charge for the year | - | 27 | 27 |
| **31 December 2010** | **-** | **34** | **34** |
| Charge for the year | - | 24 | 24 |
| **31 December 2010** | **-** | **58** | **58** |
| **Balance** | | | |
| **31 December 2010** | **858** | **657** | **1,515** |
| **31 December 2011** | **858** | **2,473** | **3,331** |

Investment property includes land, residential properties and commercial properties. During 2011 the Group performed a valuation of the larger part of investment property. The estimated fair value of investment property was noted to be in range from 2,500 TLVL to 3,000 TLVL. Valuations were performed using two generally accepted methodologies in order to estimate fair value of investment properties: income approach using discounted cash flow model valuation technique and market approach using market comparables valuation method.

## 14 OTHER ASSETS

The other assets are as follows:

| | 2011 | 2011 | 2010 | 2010 |
|---|---|---|---|---|
| **LVL '000** | **Group** | **Bank** | **Group** | **Bank** |
| Deferred expenses and accrued income | 93 | 92 | 110 | 103 |
| Cash in transit | 86 | 86 | 231 | 231 |
| Other | 109 | 36 | 31 | 31 |
| Credit card transactions in progress | 36 | 36 | 99 | 99 |
| **Total** | **324** | **250** | **471** | **464** |

## 15 ASSETS HELD FOR SALE

Assets held for sale are comprised as follows:

| | Acquisition cost | Nominal value of shares | % | Date of acquisition |
|---|---|---|---|---|
| Classic investments SIA | - | 163 | 90 | 23.12.2011 |
| Kaivas Dvīņi SIA | - | 11 | 90 | 21.11.2011 |
| Skaistkalnes 4 SIA | - | 2 | 99.5 | 08.11.2011 |
| Balss N SIA | 373 | 366 | 100 | 10.06.2011 |
| Nekustamo īpašumu apsaimniekošanas Fonds-2000 SIA | - | 79 | 90 | 22.11.2011 |
| JLE SIA | - | 2 | 100 | 07.12.2011 |
| SIJĀTS SIA | - | 72 | 90 | 16.11.2011 |
| Revera K SIA | - | 349 | 90 | 12.12.2011 |
| Lero Aerohldings Limited AS | - | 457 | 90 | 07.12.2010 |
| **Kopā** | **373** | **1,501** | | |

## 16 DEMAND BALANCES DUE TO CREDIT INSTITUTIONS

Due to credit institutions are comprised as follows:

| | 2011 | 2011 | 2010 | 2010 |
|---|---|---|---|---|
| **LVL '000** | **Group** | **Bank** | **Group** | **Bank** |
| Credit institutions registered in OECD countries | 37 | 37 | 46 | 46 |
| Residents of non-OECD countries | 238 | 238 | 8,928 | 8,928 |
| **Total demand deposits** | **275** | **275** | **8,974** | **8,974** |

As at 31 December 2011 there were 4 accounts in correspondent banks (31 December 2010 - 5).

***Concentration of amounts on demand due to credit institutions***

As at 31 December 2011 and 31 December 2010, the Bank and Group had deposits with 3 and 1 credit institution, respectively, whose balances exceeded 10% of the total deposits on demand with banks and credit institutions. Gross amount of the above balances as at 31 December 2011 and 2010 was LVL 271 thousand and LVL 8 853 thousand, respectively.

## 17 CUSTOMERS' DEPOSITS

| LVL '000 | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| **Sector profile:** | | | | |
| **Deposits from the public** | | | | |
| Legal entities | 81,094 | 81,106 | 77,078 | 77,132 |
| Individuals | 34,358 | 34,358 | 24,206 | 24,206 |
| State institutions | 14,728 | 14,728 | 131 | 131 |
| **Total deposits from the public:** | **130,180** | **130,192** | **101,415** | **101,469** |
| **Total deposits** | **130,180** | **130,192** | **101,415** | **101,469** |
| **Geographical profile:** | | | | |
| Residents | 33,867 | 33,879 | 24,361 | 24,415 |
| Non-residents | 96,313 | 96,313 | 77,054 | 77,054 |
| *Residents of OECD countries* | *30,728* | *30,728* | *33,547* | *33,547* |
| *Residents of non-OECD countries* | *65,585* | *65,585* | *43,507* | *43,507* |
| **Total deposits** | **130,180** | **130,192** | **101,415** | **101,469** |
| **Total current accounts and deposits from non-banking customers** | | | | |
| **Demand deposits** | | | | |
| Legal entities | 64,294 | 64,306 | 64,379 | 64,433 |
| Private individuals | 19,391 | 19,391 | 11,487 | 11,487 |
| State companies | 14,728 | 14,728 | 131 | 131 |
| **Total demand deposits** | **98,413** | **98,425** | **75,997** | **76,051** |
| **Term deposits** | | | | |
| Legal entities | 16,800 | 16,800 | 12,699 | 12,699 |
| Private individuals | 14,967 | 14,967 | 12,719 | 12,719 |
| **Total term deposits** | **31,767** | **31,767** | **25,418** | **25,418** |
| **Total current accounts and deposits from non-banking customers** | **130,180** | **130,192** | **101,415** | **101,469** |

As at 31 December 2011, the Bank maintained customer deposit balances of LVL 2 388 thousand (2010: LVL 1 176) which were blocked by the Bank as collateral for loans and other contingent liabilities.

### Concentrations of current accounts and customer deposits

As at 31 December 2011 and 31 December 2010 the Bank had no customers, whose deposits exceeded 10% of total customer short term deposits.

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

### 18 SUBORDINATED LIABILITIES

Subordinated liabilities as at 31 December 2011 comprise of loans received from five individuals (2010 from 3 individuals).

| | | | 31 December 2011, '000 LVL | | 31 December 2010, '000 LVL | |
|---|---|---|---|---|---|---|
| | **Maturity** | **Interest rate** | **Group** | **Separate** | **Group** | **Separate** |
| Loan Nr.1 (related party) | 02.09.2017 | 4% | 200 | 200 | 200 | 200 |
| Loan Nr.2(related party) | 02.09.2017 | 4% | 300 | 300 | 300 | 300 |
| Loan Nr.3(related party) | 02.09.2017 | 4% | 200 | 200 | 200 | 200 |
| Loan Nr.4(related party) | 28.12.2017 | 4% | 300 | 300 | 300 | 300 |
| Loan Nr.5 | 30.09.2016 | 3.2% | 214 | 214 | - | - |
| Loan Nr.6(related party) | 26.04.2018 | 4% | 300 | 300 | - | - |
| Loan Nr.7(related party) | 30.12.2016 | 3,5% | 351 | 351 | - | - |
| Loan Nr.8(related party) | 25.11.2018 | 3.6% | 914 | 914 | - | - |
| **Total** | | | **2,779** | **2,779** | **1 000** | **1 000** |

Subordinated loans are to be satisfied after the claims of all other creditors of the Bank, but before claims of shareholders of the Bank in case of liquidation of the Bank.

### 19 OTHER LIABILITIES

The other liabilities are as follows:

| **LVL '000** | **2011 Group** | **2011 Bank** | **2010 Group** | **2010 Bank** |
|---|---|---|---|---|
| *Money in transit* | 1,000 | 1,000 | 4,947 | 4,947 |
| Unmatched funds | 1,744 | 1,744 | 4,833 | 4,833 |
| Accrued expenses and deferred income | 108 | 76 | 18 | 11 |
| Other liabilities | 104 | 9 | 65 | - |
| **Total** | **2,956** | **2,829** | **9,863** | **9,791** |

Money in transit includes amounts requested by customers for payment with a value date of 1 January 2012 and 1 January 2011 respectively.

Unmatched funds include the received amounts for which the Bank has not matched incoming funds to its customers' accounts. Unmatched funds are clarified in 10 working days after receiving the amounts.

### 20 PROVISIONS

Provisions include provisions for unused vacations and amount to LVL 101 thousand for the Bank purposes and 102 thousand for the Group purposes (2010: LVL 97 thousand and LVL 97 thousand respectively).

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

### 21 SHARE CAPITAL

| | | 31 December 2011 | | 31 December 2010 | |
|---|---|---|---|---|---|
| | Nominal value (LVL) | Number of shares | Share capital LVL'000 | Number of shares | Share capital LVL'000 |
| Ordinary shares | 50 | 160,124 | 8,006 | 160,124 | 8,006 |

Shareholders

| | 2011 | | 2010 | |
|---|---|---|---|---|
| | Number of shares | % | Number of shares | % |
| Individuals | 9,229 | 5.76 | 9,229 | 5.76 |
| SMP Bank (Russia) | 150,821 | 94.19 | 150,821 | 94.19 |
| Other legal entities | 74 | 0.05 | 74 | 0.05 |
| **Total** | **160,124** | **100** | **160,124** | **100** |

The Bank's capital is registered and fully paid. Ordinary shares rank equally with respect to dividends, as and when they may be declared, and entitle all holders to equal voting rights at the shareholders' meeting. All shares rank equally with respect to residual assets. As at 31 December 2011, there were 8 shareholders – 2 legal persons and 6 individuals (31 December 2010: 8 – 2 legal persons and 6 individuals). The Bank's immediate parent bank is SMP Bank (Russia). Two individuals own 36.8% each of the immediate parent shares.

Reserves of LVL 105 thousand (2010: LVL 105 thousand) consist of reserves that were created upon privatization of the Bank in a accordance with statutory regulatory framework requirements which were in force at privatization date. These reserves cannot be distributed in dividends.

The use of share premium is defined by applicable Latvian legislation.

### 22 INTEREST INCOME

| | 2011 | 2011 | 2010 | 2010 |
|---|---|---|---|---|
| **LVL '000** | **Group** | **Bank** | **Group** | **Bank** |
| **Interest income on loans and receivables** | | | | |
| Loans and receivables | 2,995 | 2,939 | 2,785 | 2,716 |
| Balances due from credit institutions | 121 | 121 | 127 | 127 |
| Debt securities | 184 | 184 | 36 | 36 |
| **Total** | **3,300** | **3,244** | **2,948** | **2,879** |

Interest recognized on impaired loans during the year period ended 31 December 2011 amounts to LVL 447 thousand (31 December 2010: LVL 200 thousand).

### 23 INTEREST EXPENSE

| | 2011 | 2011 | 2010 | 2010 |
|---|---|---|---|---|
| **LVL '000** | **Group** | **Bank** | **Group** | **Bank** |
| **Interest expenses on liabilities at amortized cost:** | | | | |
| Current accounts and deposits from customers | 1,196 | 1,196 | 1,433 | 1,433 |
| Balances due to other banks | - | - | 2 | 2 |
| **Total** | **1,196** | **1,196** | **1,435** | **1,435** |

## 24 COMMISSION AND FEE INCOME

| LVL '000 | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| Commissions from money transfers, cash operations and servicing accounts | 1,670 | 1,670 | 1,401 | 1,401 |
| Fees from cards services | 287 | 287 | 221 | 221 |
| Commissions from guarantees | 243 | 243 | 210 | 210 |
| Brokerage fees | 155 | 155 | 202 | 202 |
| Other | 62 | 43 | 24 | 2 |
| **Total** | **2,417** | **2,398** | **2,058** | **2,036** |

## 25 COMMISSION AND FEE EXPENSE

| LVL '000 | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| Commissions paid to correspondent banks | 192 | 192 | 186 | 186 |
| Commissions for transactions with payment cards | 293 | 293 | 195 | 195 |
| Fees for operations with securities | 21 | 21 | 15 | 15 |
| Other | 3 | 3 | 3 | 3 |
| **Total** | **509** | **509** | **399** | **399** |

## 26 GAIN ON TRADING WITH FINANCIAL INSTRUMENTS, NET

| LVL '000 | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| Profit from currency exchange transactions | 1,319 | 1,319 | 921 | 921 |
| Proceeds/(loss) from revaluation of foreign exchange | (5) | (28) | 22 | 8 |
| Gain/(loss) on revaluation of investments | 15 | 15 | 7 | 7 |
| **Total** | **1,329** | **1,306** | **950** | **936** |

## 27 ADMINISTRATIVE EXPENSES

Salaries, wages and related social security contributions represent the basic remuneration of the employees, social security contributions as well as other remuneration. During years ended 31 December 2011 and 2010, the Group and the Bank employed on average 194 and 179 employees, respectively.

Administrative expenses are as follows:

| LVL '000 | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| Remuneration to staff | 1,534 | 1,531 | 1,368 | 1,364 |
| Rent of premises and other maintenance expenses | 535 | 535 | 500 | 500 |
| Compulsory state social security contributions | 402 | 401 | 362 | 362 |
| Professional services | 541 | 511 | 386 | 386 |
| Depreciation of property and equipment and investments in rented property and equipment | 230 | 224 | 241 | 241 |
| Salary of members of the Board and Council | 168 | 168 | 148 | 148 |
| Office expenses | 34 | 31 | 94 | 94 |
| Advertising and marketing | 26 | 26 | 30 | 30 |
| Other | 371 | 320 | 244 | 199 |
| **Total** | **3,841** | **3,747** | **3,373** | **3,324** |

## 28 TAXES

(a) Corporate income tax

| LVL '000 | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| Corporate income tax | 85 | 85 | - | - |
| Deferred tax | 1 | 1 | - | - |
| **Corporate income tax** | **86** | **86** | **-** | **-** |

(b) Corporate income tax reconciliation:

| LVL '000 | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| **Profit before tax** | 542 | 539 | 76 | 3 |
| Theoretical tax at the current rate 15% | 81 | 81 | 11 | - |
| Non-deductible expenses and exempt income | 5 | 5 | 3 | 1 |
| Utilization of unrecognized tax asset | - | - | (13) | - |
| Utilized tax relief on taxes paid abroad | (1) | (1) | (1) | (1) |
| **Corporate income tax (charge) / overpayment** | **85** | **85** | **-** | **-** |

(c) Deferred tax:

| LVL '000 | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| Temporary differences: | | | | |
| Property and equipment | 39 | 39 | 37 | 37 |
| Provisions | (15) | (15) | (14) | (14) |
| **Total** | 24 | 24 | 23 | 23 |

(d) Deferred tax asset and liabilities:

These deductible temporary differences, which have no expiry dates, are listed below at their tax effected accumulated values:

| **Bank** | **Assets** | | **Liabilities** | | **Net** | |
|---|---|---|---|---|---|---|
| **LVL '000** | **2011** | **2010** | **2011** | **2010** | **2011** | **2010** |
| Property and equipment | - | - | (39) | (37) | (39) | (37) |
| Other provisions | 15 | 14 | - | - | 15 | 14 |
| **Total deferred tax asset /(liabilities)** | **15** | **14** | **(39)** | **(37)** | **(24)** | **(23)** |
| **Recognized net deferred tax assets/(liabilities)** | **15** | **14** | **(39)** | **(37)** | **(24)** | **(23)** |

The rate of tax applicable for deferred taxes was 15% (2010: 15%).

**Movement in temporary differences during the year ended 31 December 2011.**

| **Bank** <br> **LVL '000** | **Balance as at 1 January 2011** | **Recognized in the statement of comprehensive income** | **31 December 2011** |
|---|---|---|---|
| Property and equipment | (37) | (2) | (39) |
| Provisions | 14 | 1 | 15 |
| | **(23)** | **(1)** | **(24)** |

(e) Deferred tax asset and liability for the Group:
These deductible temporary differences, which have no expiry dates, are listed below at their tax effected accumulated values:

| **Group** | **Assets** | | **Liabilities** | | **Net** | |
|---|---|---|---|---|---|---|
| **LVL '000** | **2011** | **2010** | **2011** | **2010** | **2011** | **2010** |
| Property and equipment | - | - | (39) | (37) | (39) | (37) |
| Other provisions | 15 | 14 | - | - | 15 | 14 |
| Tax losses carried forward | - | 16 | - | - | - | 16 |
| **Total deferred tax asset /(liabilities)** | **15** | **30** | **(39)** | **(37)** | **24** | **(7)** |
| Unrecognized tax losses from previous periods | - | (16) | - | - | (24) | (16) |
| **Recognized net deferred tax assets/(liabilities)** | **15** | **14** | **(39)** | **(37)** | **(24)** | **(23)** |

The rate of tax applicable for deferred taxes was 15% (2010: 15%).

**Movement in temporary differences during the year ended 31 December 2010**

| **Group**<br>**LVL '000** | **Balance as at 1 January 2011** | **Recognized in the profit and loss in the statement of comprehensive income** | **Balance sheet as at 31 December 2011** |
|---|---|---|---|
| Property and equipment | (37) | (2) | (39) |
| Provisions | 14 | 1 | 15 |
| | **(23)** | **(1)** | **(24)** |

## 29 CASH AND CASH EQUIVALENTS

| **LVL '000** | **2011 Group** | **2011 Bank** | **2010 Group** | **2010 Bank** |
|---|---|---|---|---|
| Cash | 3,014 | 3,014 | 1,935 | 1,935 |
| Short-term deposits with the Bank of Latvia | 8,092 | 8,092 | 9,455 | 9,455 |
| Deposits in other credit institutions with initial maturity less than three months | 49,623 | 49,623 | 49,644 | 49,644 |
| Due to other credit institutions with maturity less than three months | (275) | (275) | (8,974) | (8,974) |
| **Total** | **60,454** | **60,454** | **52,060** | **52,060** |

## 30 RELATED PARTY TRANSACTIONS

### *(a) Control relationships*

Related parties are defined as shareholders who have significant influence over the Bank and its subsidiary, members of the Board and Council, key Management personnel, their close relatives and companies in which they have a controlling interest as well as associated companies.

During 2011 and 2010, all related party transactions were performed on an arm's length basis.

Transactions with SMP Bank (Russia) for year ended 31 December are as follows:

| **LVL '000** | **2011 Group/Bank** | **Average rate** | **2010 Group/Bank** | **Average rate** |
|---|---|---|---|---|
| Due from SMP Bank (Russia) | 5,732 | 2.3% | 1,852 | 1.9% |
| Due from SMP Bank (Russia) | 186 | 0.0% | 8,853 | 0.0% |

The Bank and the Group have received subordinated loans from related parties amounted to 2,565 TLVL as at 31 December 2011. For more detailed information refer to Note 18.

## BANK’S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

Transactions with SMP Finance SIA (Latvia) for year ended 31 December 2011 are as follows:

| LVL ‘000 | 2011 Bank | Average rate | 2010 Bank | Average rate |
|---|---|---|---|---|
| Loans to AS “SMP Finance” | 11,729 | 1.87% | 6,353 | 2.11% |
| Deposits from AS “SMP Finance” | 12 | - | 54 | - |

Transactions with SMP Finance SIA (Latvia) subsidiaries held for sale for year ended 31 December 2011 are as follows (for details refer to Note 15):

**Bank**

| LVL ‘000 | Loan issued | Accrued interests | Received interests |
|---|---|---|---|
| Classic investments SIA | 169 | - | 4 |
| Kaivas Dvīņi SIA | 238 | - | 14 |
| Skaistkalnes 4 SIA | 176 | - | 4 |
| Balss N SIA | 5 | - | - |
| Nekustamo īpašumu apsaimniekošanas Fonds-2000 SIA | 142 | - | 10 |
| JLE SIA | 48 | - | - |
| SIJĀTS SIA | 1,417 | - | - |
| Lero Aeroholdings Limites AS | 1,648 | 2 | 59 |

The total amount of related party loans and deposits at the reporting year end:

| LVL ‘000 | 2011 Bank | Average rate | 2010 Bank | Average rate |
|---|---|---|---|---|
| **Deposits from SMP Bank (Russia); SMP Finance and other related parties** | **11,029** | **0.0%** | **8,907** | **0.0%** |
| **Loans to other related parties** | | | | |
| Opening balance | 600 | | 531 | |
| Loans issued during the reporting year | 26 | | 115 | |
| Loans issued during the reporting year | (26) | | (46) | |
| **Loans closing balance** | **600** | **4.0%** | **600** | **4.5%** |

Remuneration to the Board and Council members

| LVL ‘000 | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| Remuneration to the Board and Council members | 168 | 168 | 148 | 148 |
| **Total** | **168** | **168** | **148** | **148** |

Transactions with related parties for year ended 31 December 2011 are as follows:

| LVL ‘000 | 2011 Group | 2011 Bank | 2010 Group | 2010 Bank |
|---|---|---|---|---|
| Interest income | 198 | 198 | 102 | 102 |
| Interest expense | (19) | (19) | (2) | (2) |
| **Total** | **179** | **179** | **100** | **100** |

## 31 ASSETS AND LIABILITIES UNDER TRUST MANAGEMENT

| | 2011 | 2011 | 2010 | 2010 |
|---|---|---|---|---|
| **Assets '000 LVL** | **Group** | **Bank** | **Group** | **Bank** |
| Due from credit institutions | 38,080 | 38,080 | - | - |
| Fiduciary loan | 4,712 | 4,712 | 3,691 | 3,691 |
| Bonds quoted in CIS countries | 9 | 9 | 15 | 15 |
| **Total** | **42,801** | **42,801** | **3,706** | **3,706** |

| | 2011 | 2011 | 2010 | 2010 |
|---|---|---|---|---|
| **Liabilities '000 LVL** | **Group** | **Bank** | **Group** | **Bank** |
| Funds received from individuals | 150 | 150 | 15 | 15 |
| Funds received from corporate customers | 42,651 | 42,651 | 3,691 | 3,691 |
| **Total** | **42,801** | **42,801** | **3,706** | **3,706** |

Managed liabilities consist of customers' – non resident funds in total amount LVL 42,651 thousand and customers' – resident funds in total amount LVL 150 thousand.

Fiduciary loan is connected with the transaction under which the Group and the Bank have attracted resources in the form of a fiduciary deposit issued to the borrower indicated by the depositors and at depositor's risk. Customers assets are managed separately from those of the Group and the Bank in separate accounts with credit institutions acting as intermediaries in asset investment. Assets under management often represent a securities portfolio separated from the Bank's and the Group's assets, which is treated as a joint management object with its own structure, liquidity degree, sources of resources, yield and common risk. The Group and the Bank is engaged in securities purchase and sales on behalf of their customers. These securities are not disclosed in the statement of financial position of the Group and the Bank.

## 32 CONTINGENT LIABILITIES

At any time the Bank has outstanding commitments to extend the maturity of the loans issued. These commitments take the form of approved loans and credit card limits and overdraft facilities.

The Bank provides financial guarantees and letters of credit to guarantee the performance of customers to third parties. These agreements have fixed limits and generally extend for a period of up to 10 years. The Bank also provides guarantees by acting as settlement agent in securities borrowing and lending transactions.

The contractual amounts of commitments are set out in the following table by category. The amounts reflected in the table for commitments assume that amounts are fully advanced. The amounts reflected in the table for guarantees and letters of credit represent the maximum exposure that would be recognised in the statement of comprehensive income date if counterparties failed completely to perform as contracted.

| | 2011 | 2011 | 2010 | 2010 |
|---|---|---|---|---|
| **LVL '000** | **Group** | **Bank** | **Group** | **Bank** |
| Loans and credit lines commitments | 5,747 | 5,747 | 3,138 | 2,902 |
| Guarantees and letters of credit | 7,692 | 7,692 | 4,349 | 4,349 |
| **Total** | **13,439** | **13,439** | **7,487** | **7,251** |

## 33 GEOGRAPHICAL CONCENTRATION OF ASSETS, LIABILITIES, EQUITY AND CONTINGENT LIABILITIES

The geographical segmentation of the Group's and the Bank's assets, liabilities and contingent liabilities as at 31 December 2011 was as follows:

### Group

| 31 December 2011 | Latvia | OECD countries | CIS countries | Other countries | Total |
|---|---|---|---|---|---|
| **Assets '000 LVL** | | | | | |
| Cash and due from the Bank of Latvia | 10,853 | - | - | 253 | 11,106 |
| Latvian government bonds with fixed income | 3,498 | - | - | - | 3,498 |
| Fixed income debt securities | - | - | 2,553 | - | 2,553 |
| Demand deposits with credit institutions | 11,573 | 23,763 | 3,991 | 6,556 | 45,883 |
| Loans and receivables | 61,909 | 6,680 | 6,211 | 2,830 | 77,630 |
| *Loans and term deposits with credit institutions* | - | *2,094* | *5,051* | - | *7,145* |
| *Loans* | *61,909* | *4,586* | *1,160* | *2,830* | *70,485* |
| Financial assets held for trading | 35 | - | - | - | 35 |
| Property and equipment | 709 | - | - | 34 | 743 |
| Investment property | 3,331 | - | - | - | 3,331 |
| Other tax assets | 4 | - | - | - | 4 |
| Other assets and assets held for sale | 659 | - | 14 | 24 | 697 |
| **Total assets** | **92,571** | **30,443** | **12,769** | **9,697** | **145,480** |

| 31 December 2011 | Latvia | OECD countries | CIS countries | Other countries | Total |
|---|---|---|---|---|---|
| **Liabilities '000 LVL** | | | | | |
| Due on demand to credit institutions | - | 37 | 238 | - | 275 |
| Customers' deposits | 33,683 | 30,728 | 23,648 | 42,121 | 130,180 |
| Subordinated liabilities | 351 | - | 2,428 | - | 2,779 |
| Other liabilities | 2,956 | - | - | - | 2,956 |
| Other taxes and social contributions | 41 | - | - | - | 40 |
| Provisions | 98 | - | - | 4 | 102 |
| Deferred tax liability | 24 | - | - | - | 24 |
| Corporate income tax | 85 | - | - | - | 86 |
| Capital and reserves | 1,362 | - | 7,676 | - | 9,038 |
| **Total liabilities and shareholders' equity** | **38,600** | **30,765** | **33,990** | **42,125** | **145,480** |
| | | | | | |
| **Contingent liabilities** | **7,461** | **3,305** | **-** | **2,673** | **13,439** |

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

### 33 GEOGRAPHICAL CONCENTRATION OF ASSETS, LIABILITIES, EQUITY AND FORESEEABLE AND CONTINGENT (CONTINUED)

**Bank**

| 31 December 2011 | Latvia | OECD countries | CIS countries | Other countries | Total |
|---|---|---|---|---|---|
| **Assets '000 LVL** | | | | | |
| Cash and due from the Bank of Latvia | 10,853 | - | - | 253 | 11,106 |
| Latvian government bonds with fixed income | 3,498 | - | - | - | 3,498 |
| Fixed income MFI debt securities | - | - | 2,553 | - | 2,553 |
| Demand deposits with credit institutions | 11,573 | 23,763 | 3,991 | 6,556 | 45,883 |
| Loans and receivables | 65,614 | 6,680 | 6,211 | 2,830 | 81,335 |
| *Loans and term deposits with credit institutions* | - | *2,094* | *5,051* | - | *7,145* |
| *Loans* | *65,614* | *4,586* | *1,160* | *2,830* | *74,190* |
| Financial assets held for trading | 35 | - | - | - | 35 |
| Property and equipment | 641 | - | - | 34 | 675 |
| Other tax assets | 4 | - | - | - | 4 |
| Other assets | 212 | - | 14 | 24 | 250 |
| **Total assets** | **92,430** | **30,443** | **12,769** | **9,697** | **145,339** |

| 31 December 2011 | Latvia | OECD countries | CIS countries | Other countries | Total |
|---|---|---|---|---|---|
| **Liabilities '000 LVL** | | | | | |
| Due on demand to credit institutions | - | 37 | 238 | - | 275 |
| Customers' deposits | 33,695 | 30,728 | 23,648 | 42,121 | 130,192 |
| Subordinated liabilities | 351 | - | 2,428 | - | 2,779 |
| Other liabilities | 2,829 | - | - | - | 2,829 |
| Other taxes and social contributions | 9 | - | - | - | 8 |
| Provisions | 97 | - | - | 4 | 101 |
| Deferred tax liability | 24 | - | - | - | 24 |
| Corporate income tax | 86 | - | - | - | 86 |
| Capital and reserves | 1,369 | - | 7,676 | - | 9,045 |
| **Total liabilities and shareholders' equity** | **38,459** | **30,765** | **33,990** | **42,125** | **145,339** |
| | | | | | |
| **Contingent liabilities** | **7,461** | **3,305** | **-** | **2,673** | **13,439** |

## 33 GEOGRAPHICAL CONCENTRATION OF ASSETS, LIABILITIES, EQUITY AND FORESEEABLE AND CONTINGENT (CONTINUED)

The geographical segmentation of the Group's and Bank's assets, liabilities and contingent liabilities against customers as at 31 December 2010 was as follows:

**Group**

| **31 December 2010** | **Latvia** | **OECD countries** | **CIS countries** | **Other countries** | **Total** |
|---|---|---|---|---|---|
| **Assets '000 LVL** | | | | | |
| Cash and due from the Bank of Latvia | 11,390 | - | - | - | 11,390 |
| Latvian government bonds with fixed income | 3,103 | - | - | - | 3,103 |
| Demand deposits with credit institutions | 191 | 45,369 | 658 | 47 | 46,265 |
| Loans and receivables | 58,258 | 5,662 | 2,208 | 301 | 66,429 |
| *Loans and term deposits with credit institutions* | *1,000* | *2,862* | *1,524* | - | *5,386* |
| *Loans* | *57,258* | *2,800* | *684* | *301* | *61,043* |
| Financial assets held for trading | 20 | - | - | - | 20 |
| Property and equipment | 721 | - | - | - | 721 |
| Investment property | 1,515 | - | - | - | 1,515 |
| Other tax assets | 58 | - | - | - | 58 |
| Other assets | 465 | - | 6 | - | 471 |
| **Total assets** | **75,721** | **51,031** | **2,872** | **348** | **129,972** |

| **31 December 2010** | **Latvia** | **OECD countries** | **CIS countries** | **Other countries** | **Total** |
|---|---|---|---|---|---|
| **Liabilities '000 LVL** | | | | | |
| Due on demand to credit institutions | - | 46 | 8,928 | - | 8,974 |
| Customers' deposits | 24,361 | 33,547 | 5,543 | 37,964 | 101,415 |
| Subordinated liabilities | - | - | 1,000 | - | 1,000 |
| Other liabilities | 9,863 | - | - | - | 9,863 |
| Other taxes and social contributions | 18 | - | - | - | 18 |
| Provisions | 97 | - | - | - | 97 |
| Deferred tax liability | 23 | - | - | - | 23 |
| Capital and reserves | 906 | - | 7,676 | - | 8,582 |
| **Total liabilities and shareholders' equity** | **35,268** | **33,593** | **23,147** | **37,964** | **129,972** |
| | | | | | |
| **Contingent liabilities** | **4,308** | **803** | **1,982** | **394** | **7,487** |

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

### 33 GEOGRAPHICAL CONCENTRATION OF ASSETS, LIABILITIES, EQUITY AND FORESEEABLE AND CONTINGENT (CONTINUED)

**Bank**

| **31 December 2010** | **Latvia** | **OECD countries** | **CIS countries** | **Other countries** | **Total** |
|---|---|---|---|---|---|
| **Assets '000 LVL** | | | | | |
| Cash and due from the Bank of Latvia | 11,390 | - | - | - | 11,390 |
| Latvian government bonds with fixed income | 3,103 | - | - | - | 3,103 |
| Demand deposits with credit institutions | 191 | 45,369 | 658 | 47 | 46,265 |
| Loans and receivables | 59,826 | 5,662 | 2,208 | 301 | 67,997 |
| *Loans and term deposits with credit institutions* | *1,000* | *2,862* | *1,524* | - | *5,386* |
| *Loans* | *58,826* | *2,800* | *684* | *301* | *62,611* |
| Financial assets held for trading | 20 | - | - | - | 20 |
| Property and equipment | 721 | - | - | - | 721 |
| Other tax assets | 4 | - | - | - | 4 |
| Other assets | 458 | - | 6 | - | 464 |
| **Total assets** | **75,713** | **51,031** | **2,872** | **348** | **129,964** |

| **31 December 2010** | **Latvia** | **OECD countries** | **CIS countries** | **Other countries** | **Total** |
|---|---|---|---|---|---|
| **Liabilities '000 LVL** | | | | | |
| Due on demand to credit institutions | - | 46 | 8,928 | - | 8,974 |
| Customers' deposits | 24,415 | 33,547 | 5,543 | 37,964 | 101,469 |
| Subordinated liabilities | - | - | 1,000 | - | 1,000 |
| Other liabilities | 9,791 | - | - | - | 9,791 |
| Other taxes and social contributions | 18 | - | - | - | 18 |
| Provisions | 97 | - | - | - | 97 |
| Deferred tax liability | 23 | - | - | - | 23 |
| Capital and reserves | 916 | - | 7,676 | - | 8,592 |
| **Total liabilities and shareholders' equity** | **35,260** | **33,593** | **23,147** | **37,964** | **129,964** |
| | | | | | |
| **Contingent liabilities** | **4,072** | **803** | **1,982** | **394** | **7,251** |

## 34 INTEREST RATE REPRICING ANALYSIS

The interest rate repricing analysis of the Group's and the Bank's financial assets and liabilities as at 31 December 2011 was as follows:

### Group

| LVL '000 | Less than 1 month | 1– 3 months | 3– 6 months | 6– 12 months | 1- 5 years | Over 5 years | Not sensitive against interest rate changes | Total |
|---|---|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | | | |
| Cash and due from the Bank of Latvia | 8,092 | - | - | - | - | - | 3,014 | 11,106 |
| Demand deposits with credit institutions | 45,883 | - | - | - | - | - | - | 45,883 |
| Latvian government bonds with fixed income | - | 181 | - | 2,242 | - | 1,075 | - | 3,498 |
| Fixed income debt securities | - | - | 1,120 | - | - | 1,433 | - | 2,553 |
| Loans and receivables | 5,755 | 2,361 | 34,977 | 26,220 | 6,959 | 1,358 | - | 77,630 |
| Non-fixed income securities | - | - | - | - | - | - | 35 | 35 |
| Other financial assets | - | - | - | - | - | - | 122 | 122 |
| **Total financial assets** | **59,730** | **2,542** | **36,097** | **28,462** | **6,959** | **3,866** | **3,171** | **140,827** |
| **Financial liabilities** | | | | | | | | |
| Due on demand to credit institutions | 275 | - | - | - | - | - | - | 275 |
| Customers' deposits | 102,685 | 8,096 | 3,911 | 12,627 | 2,420 | 83 | 358 | 130,180 |
| Subordinated liabilities | - | - | - | - | 214 | 2,565 | - | 2,779 |
| Other financial liabilities | - | - | - | - | - | - | 2,744 | 2,744 |
| **Total financial liabilities** | **102,960** | **8,096** | **3,911** | **12,627** | **2,634** | **2,648** | **3,102** | **135,978** |
| **Interest rate risk net position** | **(43,230)** | **(5,554)** | **32,186** | **15,835** | **4,325** | **1,218** | **69** | **4,849** |

## 34 INTEREST RATE REPRICING ANALYSIS (CONTINUED)

### Bank

| LVL '000 | Less than 1 month | 1– 3 months | 3– 6 months | 6– 12 months | 1- 5 years | Over 5 years | Not sensitive against interest rate changes | Total |
|---|---|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | | | |
| Cash and due from the Bank of Latvia | 8,092 | - | - | - | - | - | 3,014 | 11,106 |
| Demand deposits with credit institutions | 45,883 | - | - | - | - | - | - | 45,883 |
| Latvian government bonds with fixed income | - | 181 | - | 2,242 | - | 1,075 | - | 3,498 |
| Fixed income debt securities | - | - | 1,120 | - | - | 1,433 | - | 2,553 |
| Loans and receivables | 5,755 | 2,361 | 34,977 | 26,598 | 10,286 | 1,358 | - | 81,335 |
| Non-fixed income securities | - | - | - | - | - | - | 35 | 35 |
| Other financial assets | - | - | - | - | - | - | 122 | 122 |
| **Total financial assets** | **59,730** | **2,542** | **36,097** | **28,840** | **10,286** | **3,866** | **3,171** | **144,532** |
| **Financial liabilities** | | | | | | | | |
| Due on demand to credit institutions | 275 | - | - | - | - | - | - | 275 |
| Customers' deposits | 102,697 | 8,096 | 3,911 | 12,627 | 2,420 | 83 | 358 | 130,192 |
| Subordinated liabilities | - | - | - | - | 214 | 2,565 | - | 2,779 |
| Other financial liabilities | - | - | - | - | - | - | 2,744 | 2,744 |
| **Total financial liabilities** | **102,972** | **8,096** | **3,911** | **12,627** | **2,634** | **2,648** | **3,102** | **135,990** |
| **Interest rate risk** | **(43,242)** | **(5,554)** | **32,186** | **16,213** | **7,652** | **1,218** | **69** | **8,542** |

## 34 INTEREST RATE REPRICING ANALYSIS (CONTINUED)

The interest rate repricing analysis of the Group's and Bank's financial assets and liabilities as at 31 December 2010 was as follows:

**Group**

| LVL '000 | Less than 1 month | 1– 3 months | 3– 6 months | 6– 12 months | 1- 5 years | Over 5 years | Not sensitive against interest rate changes | Total |
|---|---|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | | | |
| Cash and due from the Bank of Latvia | 9,455 | - | - | - | - | - | 1,935 | 11,390 |
| Demand deposits with credit institutions | 46,265 | - | - | - | - | - | - | 46,265 |
| Latvian government bonds with fixed income | 125 | - | 1,992 | 986 | - | - | - | 3,103 |
| Loans and receivables | 3,268 | 2,962 | 30,972 | 19,916 | 8,794 | 517 | - | 66,429 |
| Non-fixed income securities | - | - | - | - | - | - | 20 | 20 |
| Other financial assets | - | - | - | - | - | - | 330 | 330 |
| **Total financial assets** | **59,113** | **2,962** | **32,964** | **20,902** | **8,794** | **517** | **2,285** | **127,537** |
| **Financial liabilities** | | | | | | | | |
| Due on demand to credit institutions | 8,974 | - | - | - | - | - | - | 8,974 |
| Customers' deposits | 79,256 | 5,814 | 8,512 | 7,089 | 281 | - | 463 | 101,415 |
| Subordinated liabilities | - | - | - | - | - | 1,000 | - | 1,000 |
| Other financial liabilities | - | - | - | - | - | - | 9,780 | 9,780 |
| **Total financial liabilities** | **88,230** | **5,814** | **8,512** | **7,089** | **281** | **1,000** | **10,243** | **121,169** |
| **Interest rate risk** | **(29,117)** | **(2,852)** | **24,452** | **13,813** | **8,513** | **(483)** | **(7,958)** | **6,368** |

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

### 34 INTEREST RATE REPRICING ANALYSIS (CONTINUED)

**Bank**

| LVL '000 | Less than 1 month | 1– 3 months | 3– 6 months | 6– 12 months | 1- 5 years | Over 5 years | Not sensitive against interest rate changes | Total |
|---|---|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | | | |
| Cash and due from the Bank of Latvia | 9,455 | - | - | - | - | - | 1,935 | 11,390 |
| Demand deposits with credit institutions | 46,265 | - | - | - | - | - | - | 46,265 |
| Latvian government bonds with fixed income | 125 | - | 1,992 | 986 | - | - | - | 3,103 |
| Loans and receivables | 4,836 | 2,962 | 30,972 | 19,916 | 8,794 | 517 | - | 67,997 |
| Non-fixed income securities | - | - | - | - | - | - | 20 | 20 |
| Other financial assets | - | - | - | - | - | - | 330 | 330 |
| **Total financial assets** | **60,681** | **2,962** | **32,964** | **20,902** | **8,794** | **517** | **2,285** | **129,105** |
| **Financial liabilities** | | | | | | | | |
| Due on demand to credit institutions | 8,974 | - | - | - | - | - | - | 8,974 |
| Customers' deposits | 79,310 | 5,814 | 8,512 | 7,089 | 281 | - | 463 | 101,469 |
| Subordinated liabilities | - | - | - | - | - | 1,000 | - | 1,000 |
| Other financial liabilities | - | - | - | - | - | - | 9,780 | 9,780 |
| **Total financial liabilities** | **88,284** | **5,814** | **8,512** | **7,089** | **281** | **1,000** | **10,243** | **121,223** |
| **Interest rate risk** | **(27,603)** | **(2,852)** | **24,452** | **13,813** | **8,513** | **(483)** | **(7,958)** | **7,882** |

## 34 INTEREST RATE REPRICING ANALYSIS (CONTINUED)

*Sensitivity analysis*

The following demonstrates the sensitivity to reasonably possible changes in interest rates of the Bank's statement of comprehensive income. The analysis assumes that all other variables, in particular foreign currency rates, remain constant.

The sensitivity of statement of comprehensive income is the effect of the assumed changes in the interest rates on the net interest income for one year, following the reporting period end date, based on the floating rate non-trading financial assets and financial liabilities held at 31 December 2011 and 31 December 2010.

Sensitivity of the Group's profit and loss to changes in interest rates is not disclosed separately as it does not differ significantly from that of the Bank.

An increase and decrease of interest rates by 100 basis points would result in the following change to the statement of comprehensive income:

| | Net interest income sensitivity LVL '000 | Net interest income sensitivity LVL '000 |
|---|---|---|
| **31 December 2011** | | |
| **Aggregate impact** | **(219)** | **219** |
| **31 December 2010** | | |
| **Aggregate impact** | **(101)** | **101** |

## 35 CURRENCY ANALYSIS

The Group and the Bank actively controls foreign exchange open positions. The Bank operates based on the Law on Credit Institutions stating that the open position in any currency should not exceed 10% of shareholders' equity and that the total open position should not exceed 20% of the shareholders' equity.

The currency analysis of the Group's and the Bank's financial assets, liabilities and contingent liabilities as at 31 December 2011 was as follows:

**Group**

| | LVL | USD | EUR | Other | Total |
|---|---|---|---|---|---|
| **31 December 2011** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** |
| **Financial assets** | | | | | |
| Cash and due from the Bank of Latvia | 7,615 | 443 | 2,716 | 332 | 11,106 |
| Demand deposits with credit institutions | 8,000 | 24,128 | 5,817 | 7,938 | 45,883 |
| Latvian government bonds with fixed income | 2,955 | 543 | - | - | 3,498 |
| Fixed income debt securities | - | 2,553 | - | - | 2,553 |
| Loans and receivables | 10,490 | 19,190 | 43,649 | 4,301 | 77,630 |
| *Loans* | *9,740* | *17,096* | *43,649* | - | *70,485* |
| *Loans and term deposits with credit institutions* | *750* | *2,094* | - | *4,301* | *7,145* |
| Financial assets held for trading | 35 | - | - | - | 35 |
| Other financial assets | - | 5 | 80 | 37 | 122 |
| **Total assets** | **29,095** | **46,862** | **52,262** | **12,608** | **140,827** |
| | | | | | |
| **Financial liabilities** | | | | | |
| Due on demand to credit institutions | 37 | 154 | 84 | - | 275 |
| Customers' deposits | 23,544 | 48,982 | 45,208 | 12,446 | 130,180 |
| Subordinated liabilities | 1,300 | - | 1,479 | - | 2,779 |
| Other financial liabilities | 389 | 1,870 | 388 | 97 | 2,744 |
| **Total financial liabilities** | **25,270** | **51,006** | **47,159** | **12,543** | **135,978** |
| | | | | | |
| Net open position in the statement of financial position | 3,825 | (4,144) | 5,103 | 65 | 4,849 |
| Net position from foreign exchange – contractual amounts | 537 | 4,462 | (4,999) | - | - |
| **Net open position total** | **4,362** | **318** | **104** | **65** | **4,849** |

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

### 35 CURRENCY ANALYSIS (CONTINUED)

**Bank**

| | LVL | USD | EUR | Other | Total |
|---|---|---|---|---|---|
| **31 December 2011** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** |
| **Financial assets** | | | | | |
| Cash and due from the Bank of Latvia | 7,615 | 443 | 2,716 | 332 | 11,106 |
| Demand deposits with credit institutions | 8,000 | 24,128 | 5,817 | 7,938 | 45,883 |
| Latvian government bonds with fixed income | 2,955 | 543 | - | - | 3,498 |
| Fixed income debt securities | - | 2,553 | - | - | 2,553 |
| Loans and receivables | 15,106 | 18,888 | 43,040 | 4,301 | 81,335 |
| *Loans* | *14,356* | *16,794* | *43,040* | - | *74,190* |
| *Loans and term deposits with credit institutions* | *750* | *2,094* | - | *4,301* | *7,145* |
| Financial assets held for trading | 35 | - | - | - | 35 |
| Other financial assets | - | 5 | 80 | 37 | 122 |
| **Total financial assets** | **33,711** | **46,560** | **51,653** | **12,608** | **144,532** |
| **Financial liabilities** | | | | | |
| Due on demand to credit institutions | 37 | 154 | 84 | - | 275 |
| Customers' deposits | 23,545 | 48,987 | 45,214 | 12,446 | 130,192 |
| Subordinated liabilities | 1,300 | - | 1,479 | - | 2,779 |
| Other financial liabilities | 389 | 1,870 | 388 | 97 | 2,744 |
| **Total financial liabilities** | **25,271** | **51,011** | **47,165** | **12,543** | **135,990** |
| Net open position in the statement of financial position | 8,440 | (4,451) | 4,488 | 65 | 8,542 |
| Net position from foreign exchange – contractual amounts | 537 | 4,462 | (4,999) | - | - |
| **Net open position total** | **8,977** | **11** | **(511)** | **65** | **8,542** |

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

### 35 CURRENCY ANALYSIS (CONTINUED)

The currency analysis of the Group's and the Bank's financial assets, liabilities and contingent liabilities items as at 31 December 2010 was as follows:

**Group**

| | LVL | USD | EUR | Other | Total |
|---|---|---|---|---|---|
| **31 December 2010** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** |
| **Financial assets** | | | | | |
| Cash and due from the Bank of Latvia | 9,978 | 194 | 1,090 | 128 | 11,390 |
| Demand deposits with credit institutions | - | 31,245 | 14,698 | 322 | 46,265 |
| Latvian government bonds with fixed income | 3,103 | - | - | - | 3,103 |
| Loans and receivables | 5,277 | 15,248 | 45,130 | 774 | 66,429 |
| *Loans* | *3,527* | *12,386* | *45,130* | - | *61,043* |
| *Loans and term deposits with credit institutions* | *1,750* | *2,862* | - | *774* | *5,386* |
| Financial assets held for trading | 20 | - | - | - | 20 |
| Other financial assets | 135 | 2 | 179 | 14 | 330 |
| **Total financial assets** | **18,513** | **46,689** | **61,097** | **1,238** | **127,537** |
| | | | | | |
| **Financial liabilities** | | | | | |
| Due on demand to credit institutions | 46 | 4,582 | 4,346 | - | 8,974 |
| Customers' deposits | 11,350 | 48,777 | 40,543 | 745 | 101,415 |
| Subordinated liabilities | 1,000 | - | - | - | 1,000 |
| Other liabilities | 149 | 5,141 | 4,439 | 51 | 9,780 |
| **Total financial liabilities** | **12,545** | **58,500** | **49,328** | **796** | **121,169** |
| | | | | | |
| Net open position in the statement of financial position | 5,968 | (11,811) | 11,769 | 442 | 6,368 |
| Net position from foreign exchange – contractual amounts | 274 | 11,890 | (11,807) | (357) | - |
| **Net open position total** | **6,242** | **79** | **(38)** | **799** | **6,368** |

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

### 35 CURRENCY ANALYSIS (CONTINUED)

**Bank**

| | LVL | USD | EUR | Other | Total |
|---|---|---|---|---|---|
| **31 December 2010** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** |
| **Financial assets** | | | | | |
| Cash and due from the Bank of Latvia | 9,978 | 194 | 1,090 | 128 | 11,390 |
| Demand deposits with credit institutions | - | 31,245 | 14,698 | 322 | 46,265 |
| Latvian government bonds with fixed income | 3,103 | - | - | - | 3,103 |
| Loans and receivables | 7,381 | 15,143 | 44,699 | 774 | 67,997 |
| *Loans* | *5,631* | *12,281* | *44,699* | - | *62,611* |
| *Loans and term deposits with credit institutions* | *1,750* | *2,862* | - | *774* | *5,386* |
| Financial assets held for trading | 20 | - | - | - | 20 |
| Other financial assets | 135 | 2 | 179 | 14 | 330 |
| **Total assets** | **20,617** | **46,584** | **60,666** | **1,238** | **129,105** |
| | | | | | |
| **Financial liabilities** | | | | | |
| Due on demand to credit institutions | 46 | 4,582 | 4,346 | - | 8,974 |
| Customers' deposits | 11,359 | 48,791 | 40,574 | 745 | 101,469 |
| Subordinated liabilities | 1,000 | - | - | - | 1,000 |
| Other financial liabilities | 164 | 5,141 | 4,424 | 51 | 9,780 |
| **Total financial liabilities** | **12,569** | **58,514** | **49,344** | **796** | **121,223** |
| | | | | | |
| Net open position in the statement of financial position | 8,048 | (11,930) | 11,322 | 442 | 7,882 |
| Net position from foreign exchange – contractual amounts | 274 | 11,890 | (11,807) | (357) | - |
| **Net open position total** | **8,322** | **(40)** | **(485)** | **799** | **7,882** |

## 36 MATURITY ANALYSIS OF ASSETS AND LIABILITIES

The below amounts represent the financial assets and liabilities grouped by residual maturity.

Liquidity risk is managed by the Finance Operation Department based on the liquidity management policy. All departments whose operations affect the liquidity of the Group and the Bank are involved in liquidity management. The structure of assets/liabilities and the difference between them are calculated in order to carry out liquidity control. Liquidity is largely managed by using monetary instruments.

The maturity analysis of the Group' s and Bank's financial assets and liabilities as at 31 December 2011 was as follows:

**Group**

| | Within 1 month | 1 to 3 months | 3 to 6 months | 6 to 12 months | Over 1 year | Over 5 years or not determined | Total |
|---|---|---|---|---|---|---|---|
| **31 December 2011** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** |
| **Financial assets** | | | | | | | |
| Cash and due from the Bank of Latvia | 11,106 | - | - | - | - | - | 11,106 |
| Demand deposits with credit institutions | 45,883 | - | - | - | - | - | 45,883 |
| Latvian government bonds with fixed income | - | 181 | - | 2,242 | - | 1,075 | 3,498 |
| Fixed income debt securities | - | - | 1,120 | - | - | 1,433 | 2,553 |
| Loans and receivables | 5,410 | 2,092 | 2,956 | 29,953 | 26,110 | 11,109 | 77,630 |
| *Loans and term deposits with credit institutions* | *3,740* | - | *750* | *2,655* | - | - | *7,145* |
| *Loans* | *1,670* | *2,092* | *2,206* | *27,298* | *26,110* | *11,109* | *70,485* |
| Financial assets held for trading | 35 | - | - | - | - | - | 35 |
| Other financial assets | 122 | - | - | - | - | - | 122 |
| **Total financial assets** | **62,556** | **2,273** | **4,076** | **32,195** | **26,110** | **13,617** | **140,827** |
| | | | | | | | |
| **Financial liabilities** | | | | | | | |
| Due on demand to credit institutions | 275 | - | - | - | - | - | 275 |
| Customers' deposits | 102,778 | 8,147 | 3,967 | 12,736 | 2,552 | - | 130,180 |
| Subordinated liabilities | - | - | - | - | 215 | 2,564 | 2,779 |
| Other liabilities | 2,744 | - | - | - | - | - | 2,744 |
| **Total financial liabilities** | **105,797** | **8,147** | **3,967** | **12,736** | **2,767** | **2,564** | **135,978** |
| **Liquidity risk** | **(43,241)** | **(5,874)** | **109** | **19,459** | **23,343** | **11,053** | **4,849** |

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

### 36 MATURITY ANALYSIS OF ASSETS AND LIABILITIES (CONTINUED)

**Bank**

| | Within 1 month | 1 to 3 months | 3 to 6 months | 6 to 12 months | Over 1 year | Over 5 years or not determined | Total |
|---|---|---|---|---|---|---|---|
| **31 December 2011** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** |
| **Financial assets** | | | | | | | |
| Cash and due from the Bank of Latvia | 11,106 | - | - | - | - | - | 11,106 |
| Demand deposits with credit institutions | 45,883 | - | - | - | - | - | 45,883 |
| Latvian government bonds with fixed income | - | 181 | - | 2,242 | - | 1,075 | 3,498 |
| Fixed income debt securities | - | - | 1,120 | - | - | 1,433 | 2,553 |
| Loans and receivables | 5,410 | 2,092 | 2,956 | 30,331 | 29,437 | 11,109 | 81,335 |
| *Loans and term deposits with credit institutions* | *3,740* | - | *750* | *2,655* | - | - | *7,145* |
| *Loans* | *1,670* | *2,092* | *2,206* | *27,676* | *29,437* | *11,109* | *74,190* |
| Financial assets held for trading | 35 | - | - | - | - | - | 35 |
| Other financial assets | 122 | - | - | - | - | - | 122 |
| **Total financial assets** | **62,556** | **2,273** | **4,076** | **32,573** | **29,437** | **13,617** | **144,532** |
| | | | | | | | |
| **Financial liabilities** | | | | | | | |
| Due on demand to credit institutions | 275 | - | - | - | - | - | 275 |
| Customers' deposits | 102,790 | 8,147 | 3,967 | 12,736 | 2,552 | - | 130,192 |
| Subordinated liabilities | - | - | - | - | 215 | 2,564 | 2,779 |
| Other financial liabilities | 2,744 | - | - | - | - | - | 2,744 |
| **Total financial liabilities** | **105,809** | **8,147** | **3,967** | **12,736** | **2,767** | **2,564** | **135,990** |
| | | | | | | | |
| **Liquidity risk** | **(43,253)** | **(5,874)** | **109** | **19,837** | **26,670** | **11,053** | **8,542** |

## BANK'S SEPARATE AND CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

### 36 MATURITY ANALYSIS OF ASSETS AND LIABILITIES (CONTINUED)

The maturity analysis of the Bank's assets and liabilities as at 31 December 2010 was as follows:

**Group**

| | Within 1 month | 1 to 3 months | 3 to 6 months | 6 to 12 months | Over 1 year | Over 5 years or not determined | Total |
|---|---|---|---|---|---|---|---|
| **31 December 2010** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** |
| **Financial assets** | | | | | | | |
| Cash and due from the Bank of Latvia | 11,390 | - | - | - | - | - | 11,390 |
| Demand deposits with credit institutions | 46,265 | - | - | - | - | - | 46,265 |
| Latvian government bonds with fixed income | 125 | - | 1,992 | 986 | - | - | 3,103 |
| Loans and receivables | 5,039 | 2,962 | 3,598 | 12,695 | 29,301 | 12,834 | 66,429 |
| *Loans and term deposits with credit institutions* | *3,379* | - | *750* | *1,257* | - | - | *5,386* |
| *Loans* | *1,160* | *2,962* | *2,848* | *11,438* | *29,301* | *12,834* | *61,043* |
| Financial assets held for trading | 20 | - | - | - | - | - | 20 |
| Other financial assets | 330 | - | - | - | - | - | 330 |
| **Total financial assets** | **63,169** | **2,962** | **5,590** | **13,681** | **29,301** | **12,834** | **127,537** |
| **Financial liabilities** | | | | | | | |
| Due on demand to credit institutions | 8,974 | - | - | - | - | - | 8,974 |
| Customers' deposits | 79,367 | 5,876 | 8,715 | 7,174 | 283 | - | 101,415 |
| Subordinated liabilities | - | - | - | - | - | 1,000 | 1,000 |
| Other financial liabilities | 9,780 | - | - | - | - | - | 9,780 |
| **Total financial liabilities** | **98,121** | **5,876** | **8,715** | **7,174** | **283** | **1,000** | **121,169** |
| **Liquidity risk** | **(34,952)** | **(2,914)** | **(3,125)** | **6,507** | **29,018** | **11,834** | **6,368** |

## 36 MATURITY ANALYSIS OF ASSETS AND LIABILITIES (CONTINUED)

### Bank

| | Within 1 month | 1 to 3 months | 3 to 6 months | 6 to 12 months | Over 1 year | Over 5 years or not determined | Total |
|---|---|---|---|---|---|---|---|
| **31 December 2010** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** |
| **Financial assets** | | | | | | | |
| Cash and due from the Bank of Latvia | 11,390 | - | - | - | - | - | 11,390 |
| Demand deposits with credit institutions | 46,265 | - | - | - | - | - | 46,265 |
| Latvian government bonds with fixed income | 125 | - | 1,992 | 986 | - | - | 3,103 |
| Loans and receivables | 4,828 | 2,962 | 3,539 | 16,777 | 29,417 | 10,474 | 67,997 |
| *Loans and term deposits with credit institutions* | *3,379* | - | *750* | *1,257* | - | - | *5,386* |
| *Loans* | *1,449* | *2,962* | *2,789* | *15,520* | *29,417* | *10,474* | *62,611* |
| Financial assets held for trading | 20 | - | - | - | - | - | 20 |
| Other financial assets | 330 | - | - | - | - | - | 330 |
| **Total financial assets** | **62,958** | **2,962** | **5,531** | **17,763** | **29,417** | **10,474** | **129,105** |
| **Financial liabilities** | | | | | | | |
| Due on demand to credit institutions | 8,974 | - | - | - | - | - | 8,974 |
| Customers' deposits | 79,421 | 5,876 | 8,715 | 7,174 | 283 | - | 101,469 |
| Subordinated liabilities | - | - | - | - | - | 1,000 | 1,000 |
| Other financial liabilities | 9,780 | - | - | - | - | - | 9,780 |
| **Total financial liabilities** | **98,175** | **5,876** | **8,715** | **7,174** | **283** | **1,000** | **121,223** |
| **Liquidity risk** | **(35,217)** | **(2,914)** | **(3,184)** | **10,589** | **29,134** | **9,474** | **7,882** |

The amounts represent the assets and liabilities grouped by residual maturity.

## 36 MATURITY ANALYSIS OF ASSETS AND LIABILITIES (CONTINUED)

Analysis of financial liabilities' contractual undiscounted cash flows

The table below presents the cash flows payable by the Bank under both non-derivative and derivative financial liabilities by remaining contractual maturities as at 31 December 2011 and 2010.

The amounts disclosed in the table are the contractual undiscounted cash flows in comparison with the carrying amounts of financial liabilities, comprising discounted cash flows as at the reporting date.

The Group analysis of financial liabilities' contractual undiscounted cash flows has not been presented as the differences to the Bank analysis are insignificant.

| **31 December 2011** | **Carrying amounts** | **Gross nominal out flow** | **Less than 1 month** | **1– 3 months** | **3 months to 1 year** | **1-5 years** | **Over 5 years** |
|---|---|---|---|---|---|---|---|
| | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** |
| **Non-derivative financial liabilities** | | | | | | | |
| Due on demand to credit institutions | (275) | (275) | (275) | - | - | - | - |
| Customers' deposits | (130,192) | (130,957) | (102,790) | (8,167) | (17,003) | (2,997) | - |
| Subordinated liabilities | (2,779) | (3,408) | - | (8) | (65) | (589) | (2,746) |
| Other financial liabilities | (2,774) | (2,774) | (2,774) | - | - | - | - |
| **Total non-derivative financial liabilities** | **(136,020)** | **(137,414)** | **(105,839)** | **(8,175)** | **(17,068)** | **(3,586)** | **(2,746)** |
| Unrecognized credit liabilities | - | (7,141) | (7,141) | - | - | - | - |
| Guarantees and letters of credit | - | (6,298) | - | (6,298) | - | - | - |
| **Total financial liabilities** | **(136,020)** | **(150,853)** | **(112,980)** | **(14,473)** | **(17,068)** | **(3,586)** | **(2,746)** |

| **31 December 2010** | **Carrying amounts** | **Gross nominal inflow / (outflow)** | **Less than 1 month** | **1– 3 months** | **3 months to 1 year** | **1-5 years** | **Over 5 years** |
|---|---|---|---|---|---|---|---|
| | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** | **LVL '000** |
| **Non-derivative financial liabilities** | | | | | | | |
| Due on demand to credit institutions | (8,974) | (8,974) | (8,974) | - | - | - | - |
| Customers' deposits | (101,469) | (102,040) | (79,423) | (5,934) | (16,394) | (289) | - |
| Subordinated liabilities | (1,000) | (1,266) | - | - | (40) | (160) | (1,066) |
| Other financial liabilities | (9,780) | (9,780) | (9,780) | - | - | - | - |
| **Total non-derivative financial liabilities** | **(121,223)** | **(122,060)** | **(98,177)** | **(5,934)** | **(16,434)** | **(449)** | **(1,066)** |
| Unrecognized credit liabilities | - | (2,902) | (2,902) | - | - | - | - |
| Guarantees and letters of credit | - | (4,349) | (4,349) | - | - | - | - |
| **Total financial liabilities** | **(121,223)** | **(129,311)** | **(105,428)** | **(5,934)** | **(16,434)** | **(449)** | **(1,066)** |

## 37 CAPITAL ADEQUACY

The legislation of Latvia requires Latvian banks to maintain a minimum capital adequacy ratio of 8%. In November 2011 FCMC, has adjusted capital adequacy ratio requirement of the Bank to 11% effective from 1 April 2012. As at 31 December 2011 and 2010 the Bank was in compliance with the required capital adequacy ratio and the amount of minimum capital specified in the Credit Institutions Law and regulations of the Financial and Capital Market Commission.

The requirements laid down by the Financial and Capital Market Commission are generally consistent with the Basel Committee guidelines and the European Union directives for the calculation of equity to be utilised in the capital adequacy ratio. Based on the requirements set by the Financial and Capital Market Commission, the Bank's equity to be utilised in the capital adequacy ratio as at 31 December 2011 has been calculated as follows below:

| | 2011 | 2010 |
|---|---|---|
| | LVL '000 | LVL '000 |
| **Tier 1 capital** | | |
| Paid-up share capital | 8,006 | 8,006 |
| Share premium | 182 | 182 |
| Reserve capital | 105 | 105 |
| Retained earnings for the previous periods | 299 | 296 |
| **Total Tier 1 capital** | **8,592** | **8,589** |
| **Tier 2 capital** | | |
| Subordinated capital | 2,769 | 1,000 |
| Profit/(loss) of the reporting year | 453 | 3 |
| **Total Tier 2 capital** | **3,222** | **1,003** |
| **Equity to be utilised in the adequacy ratio per FCMC** | **11,814** | **9,592** |
| **Executive Summary** | | |
| Credit risk capital | 7,643 | 6,350 |
| Currency risk capital | 44 | 43 |
| Operational risk capital | 570 | 522 |
| **Total** | **8,257** | **6,915** |
| **Capital covering with share capital** | **3,557** | **2,677** |
| **Capital adequacy rate according to FCMC requirements** | **11%** | **11%** |
| **Minimal capital adequacy rate according to FCMC requirements** | **8%** | **8%** |

## 38 MAXIMUM CREDIT RISK EXPOSURE

The table below shows the maximum credit risk for the components of the statement of the financial position, including derivatives. Credit risk exposure is disclosed based on subjected to credit risk net carrying amount of statement of financial position items less doubtful loans and receivables.

The maximum credit exposures are shown gross, i.e. without taking into account any pledges and collaterals. Detailed information on the type and amount of collateral is presented in the respective notes.

The maximum credit risk exposure for the Group is not disclosed as it does not differ significantly from that of the Bank.

| | Maximum credit risk exposure | |
|---|---|---|
| | **2011** | **2010** |
| Due from the Bank of Latvia | 8,092 | 9,455 |
| Demand deposits with credit institutions | 45,883 | 46,265 |
| Latvian government bonds with fixed income | 3,498 | 3,103 |
| Fixed income MFI debt securities | 2,553 | - |
| Loans and term deposits with credit institutions | 7,145 | 5,386 |
| Loans and receivables | 74,190 | 62,611 |
| Financial assets held for trading | 35 | 20 |
| Other assets | 122 | 330 |
| **Total items of the statement of financial position subjected to credit risk** | **141,518** | **127,170** |
| Guarantees | 6,298 | 3,823 |
| Letters of credit | 1,394 | 526 |
| Credit related commitments | 5,747 | 2,902 |
| **Contingent liabilities** | **13,439** | **7,251** |
| **Maximum credit risk in total** | **154,957** | **134,421** |

As shown above, 52% from total gross maximum credit risk amount refers to loans and receivables (2010: 51%).

## 39 FAIR VALUE OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

The Bank and the Group have performed an assessment of its financial instruments, as required by IFRS 7 Financial Instruments: Disclosures, to determine whether it is practicable within the constraints of timeliness and cost to determine their fair values with sufficient reliability.

The estimated fair values of financial instruments at fair value through profit or loss and quoted available-for-sale securities are based on quoted market prices at reporting date without any deduction for transaction costs.

The estimated fair values of all other financial assets and liabilities are calculated using discounted cash flow techniques based on estimated future cash flows and discount rates for a similar instrument at the reporting date.

The estimates of fair value are intended to approximate the amount for which a financial instrument could be exchanged between knowledgeable, willing parties in an arm's length transaction. However, given the uncertainties and the use of subjective judgment, the fair value should not be interpreted as being realizable in an immediate sale of the assets or settlement of liabilities. The estimated fair values of financial instruments of the Group and Bank approximate their carrying values at 31 December 2011 and 31 December 2010, except for loans and receivables. Fair values of loans and receivables of the Group and the Bank at 31 December 2011 approximate LVL 78,625 thousand and LVL 82,330 thousand (2010: LVL 59,033 thousand and LVL 59,033 thousand) respectively.

## 40 LITIGATION

In the ordinary course of business, the Group and the Bank are subject to legal actions and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints, will not have a material adverse effect on the financial position and the results of operations of the Group or the Bank.

## 41 SUBSEQUENT EVENTS

On 19 March 2012, share capital of the Bank was increased by LVL 1,000 thousand to LVL 9,006 thousand.

On 23 March 2012 subordinated loan in the amount of LVL 1,054 thousand (EUR 1,5 million) with maturity 22 March 2019 was attracted by the Bank.