**Translation from Latvian original**

# JSC "REGIONALA INVESTICIJU BANKA"

# CONSOLIDATED AND BANK ANNUAL REPORT FOR THE YEAR ENDED 31 DECEMBER 2016

**Contents**



JSC "Regionala investiciju banka"

2 J. Alunana Street, Riga, LV 1010, Latvia

Phone: (371) 67508989

Fax: (371) 67508988

Registration number : 4000 356 3375
JSC "Regionala investiciju banka"

## REPORT OF THE MANAGEMENT

In 2016, JSC “Regionala Investiciju Banka”, legal address 2 J.Alunana Street, Riga, LV-1010, Latvia, registration number No. 4000 356 3375, credit institution operating license No.170 dated 03.10.2001continued its development in compliance with the previously approved five-year strategy. The Bank continued to raise the performance standards, which required both financial investments and additional human resources, leading to an increased number of personnel. In the second quarter of the reporting period, an independent audit by the US consultants took place in the Bank, as a result of which the Bank has received recommendations on improving the processes on prevention of laundering the proceeds from criminal activity (money laundering) and of terrorist financing, developed and agreed with the Financial and Capital Market Commission (FCMC) on the plan for implementation of recommendations. In the fourth quarter, FCMC performed an audit on compliance with the requirements of the “Law on the Prevention of Laundering the Proceeds from Criminal Activity (Money Laundering) and of Terrorist Financing” and “Regulations for Enhanced Customer Due Diligence” in the Bank’s activity, and the FCMC audit results have not been received on or before the day of the statement signing (refer to Appendix No. 26 to the Annual statement).Besides, customer service restructuring was implemented at the end of the year, the purpose of which was even more qualitative observance of “Know Your Customer” principle. Nonetheless, in 2016 operating profit (profit before deducting taxes and provisions for non-performing loans) increased by 24.5% as compared to the corresponding period of the previous year, and amounted to 8.9 million EUR. During 2016, the Bank created 5.3 million EUR provisions for non-performing loans. As a result, the Bank has closed the reporting period with 2.6 million EUR net profit whereof Visa Inc. share repurchase transaction made 1.26 million EUR net profit for the Bank, and this had a positive effect on return on equity (ROE) and return on assets (ROA) indicators, which, according to the results of the year, amounted to 7.12% and 0.50% respectively.

### General Economic Situation

Increase in geopolitical uncertainty has become the main topic of 2016 both for the whole world in general and for Latvia in particular. Numerous events have occurred, which may significantly influence further political and economic development of many countries and whole regions: the referendum in the UK on leaving the European Union, Donald Trump’s victory in presidential elections of the USA, failure of referendum on constitutional reform in Italy, military coup attempt in Turkey, activation of military activity in Syria, impeachment of president Rousseff in Brazil. A large number of problems was revealed due to the growth of political forces, reflecting discontent against the consequences of rapid globalization of the world economy and free trade regime, leading to the increase of income gap among different population segments, deindustrialization and increased migration flow, a large number of problems was revealed, the solution of which will determine the further course of geopolitical and socio-economic events all over the world. Coordination of actions among the OPEC member countries and other manufacturers allowed stabilizing oil prices, which have doubled after 27 dollars per barrel longstanding minimum achieved in January 2016. Stock market has also recovered after unsuccessful 2015 and early 2016 shocks, showing excellent dynamics for the year as a whole. Despite prices stabilization for most commodities and stock markets against the backdrop of their high volatility, the real economic growth rate continued to decline slowly. According to estimates of the International Monetary Fund, the global GDP growth rate in 2016 reached 3.1% as compared to 3.2% in 2015, and the growth rate of international trade volume decreased from 2.7% to 1.9%. With respect to the future prospects, IMF remains more optimistic, expecting acceleration of the global GDP growth rate to 3.4% in 2017 and 3.6% in 2018.

The growth rate of Latvian economy during 2016 has shown a tendency towards gradual decrease as compared to the previous year: GDP in real terms (preliminary seasonally and calendar adjusted data) has increased by 1.2% in the first quarter of 2016 (2.0% in 2015), by 0.8% in the second quarter (3.0% in 2015), by 0.3% in the third quarter (3.3% in 2015) and by 1.6% in the fourth quarter (2.3% in 2015). Mutual economic sanctions imposed by the EU and Russia, outflow of non-resident funds and poor disbursement of structural funds of the European Union have led to decrease in production volumes in the sphere of construction and transport, as well as decrease in Latvian export volumes. The Bank of Latvia expects that the final rate of real economic growth as a whole in 2016 will be 1.0% (in accordance with the preliminary seasonally and calendar adjusted data), but in 2017 it will accelerate again up to 3.0% due to more successful disbursement of structural funds of the European Union, which may serve as an incentive to investment level growth, as well as owing to increasing costs in the system of public administration, which may positively influence domestic demand. Average rate of inflation in 2016 reached 0.1%. However, it is expected that it may accelerate up to 1.6% in 2017. The principal risks, in terms of economic growth perspective, are connected with possible bureaucratic delays in disbursement of structural funds of the European Union, which may postpone economy recovery until 2018, as well as overoptimistic evaluation of external economic environment, which happened more than once over the last years.

**Report of the management** (continued)

**General Economic Situation** (continued)

At the end of December 2016 the assets of the banking sector of Latvia amounted to 29.5 billion EUR, which was 2.4 billion EUR or 7.6% less than in the end of 2015. Decline in the volume of assets has occurred mainly due to significant reduction of deposits, predominantly of foreign customers, in the banking system by 1.9 billion EUR or 8.2%. Deposit outflow has led to significant reduction of liquid securities portfolio on banks' balance sheets. Securities portfolio of central governments during the year has reduced by 1.2 billion EUR or 36.0% to 2.2 billion EUR. Despite the decline in total volume of assets, the consolidated loan portfolio of Latvian banking system increased by 3.1% during the year and reached 15.1 billion EUR (at the end of 2015 – 14.7 billion EUR).

The quality of granted loans is improving – the volume of overdue loans (exceeding 90 days) has reduced by 12.1% and at the end of 2016 reached 770 million EUR (4.8% of total loan portfolio).

Liquidity ratio of banking system at the end of the third quarter of 2016 was 61.3%. Capital adequacy indicators of Latvian banking sector significantly exceeded minimum requirements for the capital: overall capital rate of the sector (KPR) at the end of the third quarter amounted to 20.4%, the Core Tier 1 ratio (CET1), in turn, was 17.4%. Earning yields have improved – in general, during 2016 the banking sector operated with 453.8 million EUR profit as compared to 415.9 million EUR in 2015, and ROAE during 2016 has reached 14.4% as compared to 13.1% in 2015. However, profitability of Latvian banking sector remained at a high level owing to the one-time transaction on selling "Visa Europe" shares, as a result of which total gains of Latvian banks increased by more than 100 million EUR. Therefore, it will be extremely difficult to achieve the same excellent results in 2017.

**The Bank's Activity in the Reporting Year**

2016 has been a very eventful year for the Bank – a difficult one, however, at the same time, a very successful year. The Bank has retained its 10$^{th}$ rating position among Latvian commercial banks according to the volume of assets.

In early 2016 the FCMC Council registered the bond program prospectus for the Bank. Under the prospectus, the Bank obtained the right for public offering of bonds in the amount of 20 million US dollars. The program was successfully implemented in July 2016. Under the bond offering program, the Bank has successfully placed all the issued five-year subordinated bonds, thus, attracting 9 investors and investments in the amount of 20 million US dollars.

During the reporting period the Bank continued to improve the processes in the sphere of prevention of laundering the proceeds from criminal activity and of terrorist financing, making a considerable contribution to information systems development, increasing the personnel qualifications, reevaluating business risks and reviewing the Customer base, establishing more stringent requirements towards cooperation with the Customers. Refusal to cooperate with the Customers at high risk has led to the Customer base reduction, which caused decrease in the number of current accounts by 22% during the year, which, in turn, resulted in outflow of customer financial funds, causing decrease in deposits by 27% to 428.5 million EUR and, consequently, plunge of assets by 21% to 501.8 million EUR.
Despite the customer base reduction, the Bank has successfully implemented credit financing projects, outlined in the Bank's development strategy, and increased its credit portfolio (consisting of granted loans and loan granting liabilities) by almost 30%, which, as of December 31, 2016, reached its historical peak and constituted 134.5 million EUR. During the reporting period, the Customers settled the liabilities in the amount of 22.24 million EUR, at the same time the Bank granted new loans in the amount of 51.60 million EUR and signed loan agreements for 8.68 million EUR more.

One of the achievements in 2016 is new Customers acquisition by the Documentary Operations Section. Rapid export growth to new regions has been recorded, namely – to the markets of India, Pakistan and Egypt. Due to lower growth of economic activity in China, expansion of export regions positively influences risk diversification of the section. As compared to 2015, documentary operations turnover has grown by 17%, and the number of transactions has increased by 35%.

During the reporting period, the number of active payment cards decreased slightly – less than by 2%, nevertheless, payment cards transactions turnover increased by 15% and by the end of 2016 it reached 38.4 million EUR. The Bank actively continued to work on payment card acceptance service and the

**Report of the management** (continued)

**Bank's Activity during the Reporting Year** (continued)

annual turnover, as compared to the same period of the previous year, has increased by 249%, and the number of transactions has grown by 459%.

The Bank continued its dynamic work on expanding the range of investment products and successfully developed individual investment portfolio management services provision. Moreover, in 2016 the Financial and Capital Market Commission granted permission to provide the "Investment Deposit" service, which would allow the Customers to receive a higher yield as opposed to the "Classic Deposit", at the same time ensuring safety of the entire deposit amount.

Caring about comfort of potential Customers, at the beginning of the second half of the year the Bank implemented a project under which it provides opportunity to the potential Customers to pay for some banking services by any VISA/VISA Electron or MasterCard/Maestro payment card right on the Bank's website. Such technology solution has become very popular among the potential Customers.

In September of the current year the Bank finished execution of the project on implementation of card data double protection for online shopping. Now all the payment cards issued by the Bank are registered in the secure online shopping system 3D Secure. In order to approve an online purchase, payment card users are required to enter a unique one-time password, which is sent in a short message to the Customer's mobile phone.

An independent audit conducted by US consultants completed in November in 12 Latvian commercial banks, including JSC "Regionala Investiciju Banka", business model of which is mainly oriented at foreign Customer service. The purpose of this audit was assessment of the internal control system conformity with the US standards in the sphere of prevention of laundering the proceeds from criminal activity and of terrorist financing. The Bank complies with all the standards of performance established in Latvia and the EU, however, it continues to improve its internal control system, investing in both new IT solutions and its personnel training and staffing increase, and aims to correspond to the highest standards.

During the reporting period, some improvements were introduced in the sphere of IT, which facilitate and optimize both internal and external IT processes of the Bank. In September 2016, the Bank launched automatic software package for Customer analysis and Customer activity analysis, which allowed additional strengthening of the customer operations financial monitoring approach. Besides, moving to a new improved accounting program version has been implemented, and the main banking system has been upgraded.

Numerous structural changes happened in the Bank in 2016: some departments were merged into divisions, customer service reorganization was successfully implemented with the purpose to observe "Know Your Customer" principle at a higher level, laundering the proceeds from criminal activity and of terrorist financing risk management committee was created, as well as the Bank's Management Board was strengthened. On November 30, 2016, the fifth Member of the Board joined the Bank's Management Board – the director of Legal Department of Joint Stock Bank "Pivdennyi" Andriy Gomza, who now supervises such structural subdivisions as Legal Department and Debt Collection Section. The Bank staff has increased by 13% during 2016, mainly due to strengthening of the Compliance Division and IT Department.

The Bank continues to meet individual capital requirement set by the FCMC in October 2016, in the amount of 13.7%, which includes preservation of capital reserve in the amount of 2.5%. The Bank constantly maintains liquidity ratio in compliance with the FCMC minimum requirement of 60%, and as of December 31, 2016, the Bank's liquidity ratio constituted 81.33%.

In august 2016, the Bank established a subsidiary company with 6.6 million EUR registered capital – a limited liability company "Grunewald Residence" which intends to operate in the sphere of real estate.

**Report of the management** (continued)

**Profit distribution recommended by the Management Board**

The Management Board recommends not to distribute profit for the accounting year.

**Plans and Prospects for 2017**

To improve Customer service quality, to increase the number of Customers and to offer banking services that meet individual expectations of the Customers, the Bank will continue to improve Customer service, paying special attention to development of investment product and credit product segments. In 2017, the Bank will offer a new type of deposit to the Customers – the Investment deposit. The Bank intends to work actively on the launch of structured deposits programs and to develop in the area of consulting services provision in the investment sphere.

One of the priorities for 2017 is technological development. The plan involves implementation of such projects as:
- Internet Bank improvement;
- Internet Bank mobile application development, which initiated at the end of 2016 and is planned to be completed by the end of 2017;
- creation of a new, modern website of the Bank.

Olexandr Kovalsky — Chairman of the Board

Iurii Rodin — Chairman of the Council

Riga, March 10, 2017

**Report of the management** (continued)

**THE SUPERVISORY COUNCIL AND THE BOARD OF DIRECTORS OF THE BANK**

As at 31 December 2016 and as at the date of signing the accounts:

| | | Date of appointment |
|---|---|---|
| **The Council** | | |
| Iurii Rodin | Chairman of the Council | Re-elected – 24.02.2012 |
| Marks Bekkers | Deputy Chairman of the Council | Re-elected – 24.02.2012 |
| Dmitrijs Bekkers | Member of the Council | Re-elected – 24.02.2012 |
| Alla Vanetsyants | Member of the Council | Re-elected – 24.02.2012 |
| Iryna Buts | Member of the Council | Re-elected – 24.02.2012 |
| **The Board** | | |
| Olexandr Kovalsky | Chairman of the Board | 08.01.2013 |
| Daiga Muravska | Member of the Board | Re-elected – 28.06.2012 |
| Aleksandrs Jakovlevs | Member of the Board | 06.08.2014 |
| Gints Gritans | Member of the Board | 05.06.2015 |
| Andrejs Gomza | Member of the Board | 30.11.2016 |

**During 2016 there have been the following changes in the members of the Board of AS Reģionālā investīciju banka:**

On 30 November 2016 Andrejs Gomza was elected as the member of the Board.

| | |
|---|---|
| Olexandr Kovalsky | Iurii Rodin |
| Chairman of the Board | Chairman of the Council |

Riga, March 10, 2017

## STATEMENT OF RESPONSIBILITY OF THE MANAGEMENT

The Supervisory Council and the Board of Directors (hereinafter - the Management) of the Bank are responsible for the preparation of the Consolidated financial statements of the Bank and Bank's Subsidiary (hereinafter – Group) and the Bank's financial statements.

The Consolidated and Bank's financial statements pages 12 to 73 are prepared in accordance with the source documents and present fairly the financial position of the Group and the Bank as at 31 December 2016 and the results of their operations and cash flows for the reporting year 2016.

The financial statements are prepared in accordance with International Financial Reporting Standards as adopted in the European Union on a going concern basis. Appropriate accounting policies have been applied on a consistent basis. Prudent and reasonable judgements and estimates have been made by the Management in the preparation of the financial statements.

The Management of the Bank is responsible for the maintenance of proper accounting records, the safeguarding of the Bank's assets and the prevention and detection of fraud and other irregularities in the Bank. They are also responsible for operating the Bank in compliance with the Law on Credit Institutions, regulations of the Financial and Capital Market Commission, Bank of Latvia and other legislation of the Republic of Latvia applicable for credit institutions.

| | |
|---|---|
| Olexandr Kovalsky | Iurii Rodin |
| Chairman of the Board | Chairman of the Council |

Riga, 10 March 2017

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Translation from Latvian original*

# INDEPENDENT AUDITOR'S REPORT

**To the Shareholders of AS Regionala Investiciju banka**

## Report on the Financial Statements and the Consolidated Financial Statements

### Our Opinion

In our opinion, the accompanying financial statements of AS Regionala Investiciju Banka (the Bank) and consolidated financial statements of the Bank and its subsidiary (the Group) set out on pages 12 to 73 of the accompanying annual report give a true and fair view of the financial position of the Bank and the Group as at December 31, 2016, and of their financial performance and their cash flows for the year then ended in accordance with the International Financial Reporting Standards as adopted by the European Union.

### What we have audited

The Bank's and consolidated financial statements comprise:

- the Bank's and consolidated statements of financial position as at December 31, 2016,
- the Bank's and consolidated statements of comprehensive income for the year then ended,
- the Bank's and consolidated statements of changes in equity for the year then ended,
- the Bank's and consolidated statements of cash flows for the year then ended, and
- the notes to the Bank's and consolidated financial statements which include a summary of significant accounting policies.

### Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing adopted in the Republic of Latvia (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Bank's and Consolidated Financial Statements* section of our report.

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

### Independence

We are independent of the Bank and Group in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code) and with the ethical requirements and auditor's independence rules that are relevant to our audit of the Bank's and consolidated financial statements in the Republic of Latvia. We have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

### Reporting on Other Information

Management is responsible for the other information. The other information comprises

- the Report of the Management, as set out on pages 3 to 7 of the accompanying annual report,
- the Statement of Responsibility of the Management, as set out on page 8 of the accompanying annual report,

but does not include the Bank's and consolidated financial statements and our auditor's report thereon.

Our opinion on the Bank's and consolidated financial statements does not cover the other information included in the annual report, and we do not express any form of assurance conclusion thereon, except as described in the *Other Reporting Responsibilities in Accordance with the Legislation of the Republic of Latvia* section of our report.

*PricewaterhouseCoopers SIA, Kr. Valdemāra iela 21-21, Rīga, LV-1010, Latvia, LV40003142793*
*T: +371 6709 4400, F: +371 6783 0055, www.pwc.lv*

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In connection with our audit of the Bank's and consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the Bank's and consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed and in light of the knowledge and understanding of the entity and its environment obtained in the course of our audit, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

### Responsibilities of Management and Those Charged with Governance for the Bank's and Consolidated Financial Statements

Management is responsible for the preparation of the Bank's and consolidated financial statements that give a true and fair view in accordance with the International Financial Reporting Standards as adopted by the European Union and for such internal control as management determines is necessary to enable the preparation of the Bank's and consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the Bank's and consolidated financial statements, management is responsible for assessing the Bank's and the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's and Group's financial reporting process.

### Auditor's Responsibilities for the Audit of the Bank's and Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the Bank's and consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the Bank's and consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit 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 Bank's and Group's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's and Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the Bank's and consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank or the Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the Bank's and consolidated financial statements, including the disclosures, and whether the Bank's and consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

**Other Reporting Responsibilities in Accordance with the Legislation of the Republic of Latvia**

In addition, in accordance with the Law on Audit Services of the Republic of Latvia with respect to the Report of the Management, our responsibility is to consider whether the Report of the Management is prepared in accordance with the requirements of the Financial and Capital Market Commission Regulation No. 46 “Regulations on the Preparation of Annual Accounts and Consolidated Annual Accounts for Banks, Investment Brokerage Firms and Investment Management Companies”.

Based solely on the work required to be undertaken in the course of our audit, in our opinion:

- the information given in the Management Report for the financial year for which the Bank's and consolidated financial statements are prepared is consistent with the Bank's and consolidated financial statements; and
- the Management Report has been prepared, in all material respects, in accordance with the requirements of the Financial and Capital Market Commission Regulation No. 46 “Regulations on the Preparation of Annual Accounts and Consolidated Annual Accounts for Banks, Investment Brokerage Firms and Investment Management Companies”.

PricewaterhouseCoopers SIA
Certified audit company
Licence No. 5

Juris Lapše
Certified auditor in charge
Certificate No. 116
Persona per procura
Riga, Latvia
10 March 2017

* This version of our report is a translation from the original, which was prepared in Latvian. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.

Consolidated and Bank's Statement of Comprehensive Income for the year ended 31 December 2016

| | Notes | 2016 Group EUR | 2016 Bank EUR | 2015 Group EUR | 2015 Bank EUR |
|---|---|---|---|---|---|
| Interest income | 5 | 9,583,303 | 9,583,303 | 8,293,530 | 8,293,530 |
| Interest expense | 5 | (4,497,751) | (4,497,751) | (5,389,982) | (5,389,982) |
| **Net interest income** | | **5,085,552** | **5,085,552** | **2,903,548** | **2,903,548** |
| Provisions for loan impairment | 12 | (5,322,062) | (5,322,062) | (7,914,812) | (7,914,812) |
| **Net interest income after provision for loan impairment** | | **(236,510)** | **(236,510)** | **(5,011,264)** | **(5,011,264)** |
| Fee and commission income | 6 | 9,356,742 | 9,356,799 | 9,690,351 | 9,690,351 |
| Fee and commission expense | 6 | (1,318,811) | (1,318,811) | (1,483,825) | (1,483,825) |
| **Net fee and commission income** | 6 | **8,037,931** | **8,037,988** | **8,206,526** | **8,206,526** |
| Gain from sale of available for sale financial assets, net | | 1,256,507 | 1,256,507 | - | - |
| Loss from sale of financial assets at fair value through profit or loss, net | | (1,724) | (1,724) | - | - |
| Loss from revaluation of trading securities, net | | (114,742) | (114,742) | (274,675) | (274,675) |
| Loss from derivative financial instruments revaluation, net | | (48,986) | (48,986) | (1,067,896) | (1,067,896) |
| Gain from trading in foreign currencies, net | | 2,880,341 | 2,880,341 | 2,978,952 | 2,978,952 |
| Gain loss from foreign exchange translation, net | | 301,166 | 301,166 | 701,440 | 701,440 |
| Impairment loss on other assets | | (25,431) | (25,431) | (179,232) | (179,232) |
| Other operating income | 8 | 482,458 | 482,458 | 275,830 | 275,830 |
| Gain from sale of repossessed collateral | | 277,614 | 277,614 | 17,184 | 17,184 |
| Administrative expenses | 7 | (8,669,809) | (8,649,524) | (6,446,576) | (6,446,576) |
| Amortization and depreciation charges | 14, 15 | (374,129) | (374,129) | (285,658) | (285,658) |
| Other operating expense | | (200,431) | (200,431) | (146,545) | (146,545) |
| **Profit/(loss) before income tax** | | **3,564,255** | **3,584,597** | **(1,231,914)** | **(1,231,914)** |
| Corporate income tax | 9 | (1,006,442) | (1,006,442) | (337,893) | (337,893) |
| **Net profit/ (loss) for the year** | | **2,557,813** | **2,578,155** | **(1,569,807)** | **(1,569,807)** |
| *Items that can be reclassified subsequently to profit or loss:* | | | | | |
| Net gain from revaluation of investment securities available-for-sale | | - | - | 919,970 | 919,970 |
| **Total comprehensive income/ (loss) for the year attributable to the owners of the Bank** | | **2,557,813** | **2,578,155** | **(649,837)** | **(649,837)** |

The Consolidated and Bank's financial statements on pages 12 to 73 have been approved by the Supervisory Council and the Board of Directors of the Bank and signed on their behalf by:

Olexandr Kovalsky
Chairman of the Board

Iurii Rodin
Chairman of the Council

Riga, 10 March 2017

***The accompanying notes on pages 16 to 73 are an integral part of these financial statements.***

## Consolidated and Bank's Statement of Financial Position as at 31 December 2016

| | Notes | 31.12.2016 Group EUR | 31.12.2016 Bank EUR | 31.12.2015 Group EUR | 31.12.2015 Bank EUR |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| Cash and balances with the Bank of Latvia | 10 | 148,906,810 | 148,906,810 | 114,447,515 | 114,447,515 |
| Balances due from banks | 11 | 99,833,647 | 99,833,647 | 142,561,234 | 142,561,234 |
| Loans and advances to customers | 12 | 99,513,448 | 99,513,448 | 67,784,042 | 67,784,042 |
| Financial assets at fair value through profit or loss | 13 | 125,243,072 | 125,243,072 | 288,977,983 | 288,977,983 |
| Available for sale financial assets | 16 | 188,972 | 188,972 | 919,980 | 919,980 |
| Derivative financial instruments | 24 | 483,074 | 483,074 | 262,735 | 262,735 |
| Intangible assets | 14 | 524,995 | 524,995 | 255,318 | 255,318 |
| Property and equipment | 15 | 14,868,398 | 14,868,398 | 14,902,365 | 14,902,365 |
| Investment in subsidiary | | - | 6,600,000 | - | - |
| Other assets | 17 | 5,390,091 | 5,390,054 | 5,313,064 | 5,313,064 |
| Deferred expenses | | 247,214 | 247,214 | 150,868 | 150,868 |
| **Total assets** | | **495,199,721** | **501,799,684** | **635,575,104** | **635,575,104** |
| **Liabilities** | | | | | |
| Customer accounts | 19 | 421,912,801 | 428,493,320 | 583,979,790 | 583,979,790 |
| Derivative financial instruments | 24 | 1,378,768 | 1,378,768 | 1,109,443 | 1,109,443 |
| Other financial liabilities | 21 | 668,967 | 668,069 | 735,124 | 735,124 |
| Deferred income and accrued expenses | 22 | 712,986 | 712,986 | 1,136,625 | 1,136,625 |
| Debt securities | 20 | 19,072,989 | 19,072,989 | - | - |
| Subordinated loan | 34 | 14,072,281 | 14,072,281 | 13,623,927 | 13,623,927 |
| Current income tax liability | 33 | 555,683 | 555,683 | - | - |
| Deferred tax liability | 23 | 230,917 | 230,917 | 33,709 | 33,709 |
| **Total liabilities** | | **458,605,392** | **465,185,013** | **600,618,618** | **600,618,618** |
| **Equity** | | | | | |
| Share capital | 25 | 32,334,756 | 32,334,756 | 32,334,762 | 32,334,762 |
| Reserves | | 6 | 6 | - | - |
| Revaluation reserve on available-for-sale financial assets | | - | - | 919,970 | 919,970 |
| Retained earnings | | 4,259,567 | 4,279,909 | 1,701,754 | 1,701,754 |
| **Total equity** | | **36,594,329** | **36,614,671** | **34,956,486** | **34,956,486** |
| **Total liabilities and equity** | | **495,199,721** | **501,799,684** | **635,575,104** | **635,575,104** |
| **Off balance sheet items** | | | | | |
| Guarantees issued | 26 | 5,460,027 | 5,460,027 | 10,725,694 | 10,725,694 |
| Credit related commitments | 26 | 20,762,556 | 20,762,556 | 24,536,046 | 24,536,046 |
| **Assets under management** | 35 | 111,570,097 | 111,570,097 | 107,887,111 | 107,887,111 |

The Consolidated and Bank's financial statements on pages 12 to 73 have been approved by the Supervisory Council and the Board of Directors of the Bank and signed on their behalf by:

Olexandr Kovalsky
Chairman of the Board

Iurii Rodin
Chairman of the Council

Riga, 10 March 2017

***The accompanying notes on pages 16 to 73 are an integral part of these financial statements.***

## Consolidated Statement of Changes in Equity for the year ended 31 December 2016

| | Paid-in share capital | Reserves | Retained earnings | Revaluation reserve on available-for-sale financial assets | Total |
|---|---|---|---|---|---|
| | EUR | EUR | EUR | EUR | EUR |
| **Balance as at 31 December 2014** | **32,334,762** | **-** | **3,271,561** | **-** | **35,606,323** |
| Comprehensive loss for the year | - | - | (1,569,807) | 919,970 | (649,837) |
| **Balance as at 31 December 2015** | **32,334,762** | **-** | **1,701,754** | **919,970** | **34,956,486** |
| The denomination of the share capital EUR | (6) | 6 | - | - | - |
| Sale of Available-for-sale assets | - | - | - | (919,970) | (919,970) |
| Comprehensive income for the year | - | - | 2,557,813 | - | 2,557,813 |
| **Balance as at 31 December 2016** | **32,334,756** | **6** | **4,259,567** | **-** | **36,594,329** |

## Bank's Statement of Changes in Equity for the year ended 31 December 2016

| | Paid-in share capital | Reserves | Retained earnings | Revaluation reserve on available-for-sale financial assets | Total |
|---|---|---|---|---|---|
| | EUR | EUR | EUR | EUR | EUR |
| **Balance as at 31 December 2014** | **32,334,762** | **-** | **3,271,561** | **-** | **35,606,323** |
| Comprehensive loss for the year | - | - | (1,569,807) | 919,970 | (649,837) |
| **Balance as at 31 December 2015** | **32,334,762** | **-** | **1,701,754** | **919,970** | **34,956,486** |
| The denomination of the share capital EUR | (6) | 6 | - | - | - |
| Sale of Available for sale assets | - | - | - | (919,970) | (919,970) |
| Comprehensive income for the year | - | - | 2,578,155 | - | 2,578,155 |
| **Balance as at 31 December 2016** | **32,334,756** | **6** | **4,279,909** | **-** | **36,614,671** |

***The accompanying notes on pages 16 to 73 are an integral part of these financial statements.***

## Consolidated and Bank's Statement of Cash Flows for the year ended 31 December 2016

| | Notes | 2016 Group EUR | 2016 Bank EUR | 2015 Group EUR | 2015 Bank EUR |
|---|---|---|---|---|---|
| **Cash flows from operating activities** | | | | | |
| Interest received | | 10,193,843 | 10,193,843 | 5,198,813 | 5,198,813 |
| Interest paid | | (4,456,613) | (4,456,613) | (5,550,783) | (5,550,783) |
| Fees and commission received | | 9,356,742 | 9,356,799 | 9,690,351 | 9,690,351 |
| Fees and commission paid | | (1,318,811) | (1,318,811) | (1,483,825) | (1,483,825) |
| Income on sale of available for sale financial assets | | 980,702 | 980,702 | - | - |
| Income on foreign exchange | | 2,880,341 | 2,880,341 | 2,978,952 | 2,978,952 |
| Other operating income | | 482,457 | 482,457 | 275,830 | 275,830 |
| Personnel expenses paid | | (5,711,430) | (5,707,569) | (4,573,179) | (4,573,179) |
| Administrative and other operating expenses | | (2,881,196) | (2,864,772) | (2,342,427) | (2,342,427) |
| Income tax paid | | (253,551) | (253,551) | (285,021) | (285,021) |
| **Cash flows generated from operating activities before changes in operating assets and liabilities** | | **9,272,484** | **9,292,826** | **3,908,711** | **3,908,711** |
| **Changes in operating assets and liabilities** | | | | | |
| Net decrease/(increase) of securities at fair value through profit or loss | | 164,497,985 | 164,497,985 | (64,807,665) | (64,807,665) |
| Net decrease of balances due from banks | | 9,097,720 | 9,097,720 | 17,667,836 | 17,667,836 |
| Net (increase)/ decrease of loans and advances to customers | | (36,702,457) | (36,702,457) | 9,040,081 | 9,040,081 |
| Net decrease/(increase) of other assets | | 1,479,058 | 1,479,095 | (4,169,877) | (4,169,877) |
| Net decrease of customer accounts | | (169,548,464) | (162,967,945) | (8,088,150) | (8,088,150) |
| Net increase /(decrease) in other liabilities | | 39,615 | 38,717 | (1,363,003) | (1,363,003) |
| **Net cash and cash equivalents used in operating activities** | | **(21,864,059)** | **(15,264,059)** | **(47,812,067)** | **(47,812,067)** |
| **Cash flows from investing activities** | | | | | |
| Investment in subsidiary | | - | (6,600,000) | - | - |
| Purchase of intangible assets | | (358,014) | (358,014) | (88,202) | (88,202) |
| Purchase of fixed assets | | (251,827) | (251,827) | (14,843,116) | (14,843,116) |
| **Net cash and cash equivalents used in investing activities** | | **(609,841)** | **(7,209,841)** | **(14,931,318)** | **(14,931,318)** |
| **Net cash and cash equivalents used in financing activities** | | | | | |
| Issue of debt securities | | 17,794,806 | 17,794,806 | - | - |
| **Net cash and cash equivalents used in financing activities** | | **17,794,806** | **17,794,806** | **-** | **-** |
| Effect of exchange rates on cash and cash equivalents | | 5,409,256 | 5,409,256 | 15,519,582 | 15,519,582 |
| **Net increase/(decrease) in cash and cash equivalents** | | **730,162** | **730,162** | **(47,223,803)** | **(47,223,803)** |
| Cash and cash equivalents at the beginning of the year | 18 | 244,002,403 | 244,002,403 | 291,226,206 | 291,226,206 |
| **Cash and cash equivalents at the end of the year** | **18** | **244,732,565** | **244,732,565** | **244,002,403** | **244,002,403** |

***The accompanying notes on pages 16 to 73 are an integral part of these financial statements.***

## NOTES TO THE FINANCIAL STATEMENTS

### NOTE 1 INCORPORATION AND PRINCIPAL ACTIVITIES

JSC “Regionala investiciju banka” (hereinafter – the Bank) provides financial services to corporate clients and individuals. The Bank established its representative office in Odessa, Ukraine in 2005 and representative office in Dnepropetrovsk, Ukraine in 2007. In the beginning of 2009 the Bank has established representative office in Kiev, Ukraine. Furthermore, in 2010 the Bank has established its representative office in the capital of Belgium – Brussels.

In August 2016, the Bank established its 100% owned subsidiary - a limited liability company "Grunewald Residence", reg. No. 40203014344, whose share capital is EUR 6,600,000.

The Bank and the limited liability company "Grunewald Residence" together form a group (hereinafter - the Group), operating in the financial services and real estate.

The legal and officeaddress of the Bank is:
2 J. Alunana Street,
LV-1010, Riga,
Latvia

The legal and officeaddress of the SIA “Grunewald Residence” is:
2 J. Alunana Street,
LV-1010, Riga,
Latvia

The Bank has no other representative offices, subsidiaries or other entities, except for the above.

These financial statements have been approved for issue by the Bank’s Council and the Board of Directors on 10 March 2017.

### NOTE 2 OPERATING ENVIRONMENT OF THE BANK

Operations of the Bank are affected by tendencies in Ukrainian market, as largest shareholder of the Bank is Ukrainian public joint stock company bank “Pivdennij”, as well as significant portion of the loans issued by the Bank have been issued to the Ukrainian companies and companies with significant share of their revenues being generated from the operations in Ukraine.

The following table indicates total exposure of the Bank and Group in Ukraine as at 31 December 2016 and as at 31 December 2015:

| | 31.12.2016 | 31.12.2016 | 31.12.2015 | 31.12.2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | ‘000 EUR | ‘000 EUR | ‘000 EUR | ‘000 EUR |
| **Balance sheet assets subject to the Ukraine country risk:** | | | | |
| Balances due from banks | 2,281 | 2,281 | 876 | 876 |
| Loans issued | 18,358 | 18,358 | 19,960 | 19,960 |
| **Total** | **20,639** | **20,639** | **20,836** | **20,836** |
| **Off-balance sheet items subject to the Ukraine country risk:** | | | | |
| Off-balance sheet commitments to clients | 2,599 | 2,599 | 3,956 | 3,956 |
| **Total** | **2,599** | **2,599** | **3,956** | **3,956** |

Compared with 2015 and 2014, in 2016 the macroeconomic situation in Ukraine began to stabilize. Real GDP growth rates over the past year showed gradual improvement and the provisional data shows that Ukraine's economic growth rate reached 2%, compared with a decrease of 9.9% in 2015 and 6.6% in 2014. The inflation rate slowed down sharply from 43.3% in 2015 to 12.4% in 2016.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 2 OPERATING ENVIRONMENT OF THE BANK** (continued)

The main factors that helped to stabilize the economy after two years of recession, were bilateral and diverse support of creditors, improving the dynamics of prices of some exported goods, as well as the strengthening of domestic demand. As a result of reduction of short-term political uncertainty, after the appointment of the new government in April 2016, and taking into account the achievement of key targets, in September, the International Monetary Fund has decided to allocate the next tranche in the amount of USD 1 billion under the program of financial support, thereby increasing the total amount of allocated funding up to US $ 7.6 billion of planned USD 17.5 billion. Additionally, USD 1 billion Eurobonds guaranteed by the USA government were issued. As a result, during the year, the external reserves of Ukraine increased by USD 2.2 billion and reached USD 15.5 billion by the end of the year. Nevertheless, the state budget deficit is remaining significant – 3% of GDP, and the amount of government and government guaranteed liabilities increased during the year by USD 5.5 billion up to USD 71 billion. During the year, quite high volatility of the UAH exchange rate was remaining and within a year, the UAH exchange rate fell by 12% against the USD and 8% against the euro. However, in comparison with 2014 and 2015, the rate remained much more stable. With the stabilization of the exchange rate, as well as significant reduction of inflation, the National Bank of Ukraine has lowered the refinancing rate from 22% to 14% during the year.

Both Ukrainian government agencies and international institutions forecast increase in GDP growth in 2017 up to 2.3%-2.5%. In 2016, the rating agencies "Moody's" and "Standard & Poor's" confirmed the rating of Ukrainian state, in turn, the rating agency "Fitch" upgraded the Ukrainian government rating to "B-". All rating agencies indicate the stabilization of the macroeconomic situation and forecast continued growth in the years 2017 and 2018. Nevertheless, it notes that significant political and economic problems remain, which are primarily related to the conflict in the eastern regions of Ukraine, the substantial size of the debt of the country, as well as the stability of the banking and financial sector.

Stability of Banking and Financial sector remains one of the central issues on the agenda of the government and the National Bank of Ukraine. As a result of implemented government policy, there is a certain stabilization of the banking sector statistics: there is an ongoing recapitalization of the largest banks on the basis of stress tests developed by the Central Bank; the outflow of deposits from the banking sector is stopped - the volume of deposits in the solvent banks grew by 117.6 billion UAH during 2016; there was a decline in interest rates on deposits for 12 months in UAH and USD (by 3.8 percentage points to 17.5% for deposits in UAH and by 2.2 percentage points to 5.7% for deposits in USD); the liquidity of the banking sector has improved significantly as a result of the stabilization of the deposit base and the reduction of interest rates. However, the level of capitalization of the banking sector still remains low and the proportion of bad loans exceed 50% of the total credit volume of the banking sector. Undoubtedly, the highlight of 2016 was the nationalization of the country's largest bank "PrivatBank", which took place in December in order to prevent the outflow of deposits and panic. According to the National Bank of Ukraine, for the recapitalization of "PrivatBank" 148 billion UAH may be required. By mid-January, the National Bank has already directed 27.2 billion UAH for this purpose. Considering the financial result of "PrivatBank", total losses of the Ukraine's banking sector reached 159 billion UAH in 2016, compared with 66 billion UAH in 2015. Nevertheless, without taking into account the financial result of "PrivatBank", losses of other banks amounted to only 23 billion UAH. Overall, in 2016, the activities of 23 Ukrainian banks have stopped and the number of banks in the country decreased to 94 by the end of the year. In turn, after the nationalization of "PrivatBank" in December 2016, the share of state-owned banks accounted for 51.3% of the net assets of the banking system, compared to 28.1% at the beginning of the year. Summing up the situation, the International Monetary Fund concluded that the "nationalization was an important step to ensure financial stability". Speaking about the prospects and goals for 2017, the National Bank of Ukraine notes that the main task of the banking sector in the next year will be the resumption of crediting the real sector and households.

**Impact on borrowers**

Borrowers of the Bank may be affected by the lower liquidity situation which could in turn impact their ability to repay the amounts owed. Deteriorating operating conditions for borrowers may also have an impact on management's cash flow forecasts and assessment of the impairment of financial and non-financial assets. To the extent that information is available, management has properly reflected revised estimates of expected future cash flows in its impairment assessments.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 2 OPERATING ENVIRONMENT OF THE BANK** (continued)

**Impact on collateral**
The amount of provision for impaired loans is based on management's appraisals of these assets at the balance sheet date after taking into consideration the cash flows that may result from foreclosure less costs for obtaining and selling the collateral. As a result of possible economy downturn, the actual realizable value on foreclosure may differ from the value ascribed in estimating allowances for impairment.

## NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the significant accounting policies of Group and Bank, all of which have been applied consistently throughout 2016 and 2015, are set out below:

### (a) Reporting currency
The tabular amounts in the accompanying financial statements are reported in Euros (EUR), unless otherwise stated.

### (b) Basis of preparation
These financial statements are prepared in accordance with International Financial Reporting Standards as adopted by the European Union (hereinafter - IFRS), on a going concern basis. In preparation of the financial statements on a going concern basis the management considered the Group’s and Bank’s financial position, access to financial resources and analysed the impact of the recent financial crisis on the future operations of the Group and the Bank.

The financial statements are prepared under the historical cost convention as modified by the fair valuation of financial assets held at fair value through profit or loss, available-for-sale financial assets and derivative financial instruments.

The preparation of financial statements in conformity with IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on Management’s best knowledge of current events and actions, actual results ultimately may differ from those estimates.

The accounting policies used in the preparation of the financial statements for the year ended 31 December 2016 are consistent with those used in the annual financial statements for the year ended 31 December 2015.

### (c) Consolidation
Subsidiaries are those investees, that the Group controls because the Group (i) has power to direct relevant activities of the investees that significantly affect their returns, (ii) has exposure, or rights, to variable returns from its involvement with the investees, and (iii) has the ability to use its power over the investees to affect the amount of investor’s returns..

Subsidiaries are consolidated from the date on which control is transferred to the Group and excluded from the consolidated financial statements from the date that control ceases. Acquisition of subsidiaries is accounted for using the purchase method. The acquisition is measured as the assets given up, shares issued or liabilities undertaken at fair value of the purchase date, plus costs directly attributable to the acquisition. Excess of the net assets purchased over the purchase price is recorded as a goodwill. Transactions between the Group companies, rights and obligations between them and unrealized gains on transactions between Group companies are eliminated; unrealised losses are also eliminated unless costs cannot be recovered. Where necessary, accounting policies of subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

Investments in subsidiaries are stated at cost less impairment (if any) in the Bank’s financial statements.

### (d) Income and expense recognition
Interest income and expense are recognised in the statement of comprehensive income for all interest bearing instruments on an accrual basis using the effective interest method.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (continued)

**(d) Income and expense recognition** (continued)
The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability.

When loans become doubtful of collection, they are written down to their recoverable amounts and interest income is thereafter recognised based on the rate of interest that was used to discount the future cash flows for the purpose of measuring the recoverable amount.

Commissions received or incurred in respect of origination of financial assets or funding are deferred and recognised as an adjustment to the effective interest rate on the asset or liability. Commissions on servicing of settlement accounts are recognized in the comprehensive income statement on a regular basis throughout the duration of the contract with customer. Other fees and commissions, including those related to trust activities, are credited and/or charged to the statement of comprehensive income as earned / incurred.

**(e) Foreign currency translation**
*Functional and presentation currency*
The functional currency of each of the Group's consolidated entities is the currency of the primary economic environment in which the entity operates. The financial statements are presented in euros ('EUR'), which is the Bank's functional and Group's presentation currency.

*Transactions and balances*
Transactions in foreign currencies are converted into euros at the date of the transaction in the current rate, which is determined on the basis of the European system of central banks and of the other central banks of the conciliation procedure and which is published by the European Central bank website. Foreign currency exchange rate of the resulting profit or loss is included in the comprehensive income statement as a gain or loss from revaluation of foreign exchange position.

During the preparation of the financial statements of the Group and the Bank, the following currency exchanges rates were most commonly used (foreign currency units against one EUR):

| **Reporting date** | **USD** |
|---|---|
| As at 31 December 2016 | 1.0541 |
| As at 31 December 2015 | 1.0887 |

**(f) Income taxes**
Income tax is calculated in accordance with Latvian tax regulations and is based on the taxable income reported for the taxation period.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. The deferred income tax is calculated based on currently enacted tax rates that are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

The principal temporary differences arise from different rates of accounting and tax amortisation and depreciation on intangible and fixed assets, as well as accruals for employee vacation expenses. Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

**(g) Cash and cash equivalents**

Cash and cash equivalents comprise cash and demand deposits with the Bank of Latvia and other credit institutions, due to and from other credit institutions with original maturity of 3 months or less.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (continued)

**(h) Loans and provisions for loan impairment**

Loans and advances to customers are accounted for as loans and receivables. Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in active markets.

Loans and receivables are recognised initially at fair value plus transaction costs that are directly attributable to the acquisition of financial asset. Loans and receivables are subsequently carried at amortised cost using the effective interest method. All loans and receivables are recognised when cash is advanced to borrowers and derecognised on maturitys.

The Bank assesses at each balance sheet date whether there is objective evidence that loans and receivables are impaired. If any such evidence exists, the amount of the loss for loan impairment which has been incurred is measured as the difference between the asset's carrying amount and the recoverable amount, being the present value of expected cash flows (excluding future credit losses that have not been incurred), including amounts recoverable from guarantees and collateral, discounted at the original effective interest rate. The Bank does not perform collective assessment of provisions as it can carry out assessment of each individual loan taken the number of loans issued.

The primary factors that the Bank considers in determining whether a financial asset is impaired are its overdue status and realisability of related collateral, if any.

The following other principal criteria are also used to determine whether there is objective evidence that an impairment loss has occurred:

- any instalment is overdue and the late payment cannot be attributed to a delay caused by the settlement systems;
- the borrower experiences a significant financial difficulty as evidenced by the borrower's financial information that the Bank obtains;
- the borrower considers bankruptcy or a financial reorganisation;
- there is an adverse change in the payment status of the borrower as a result of changes in the national or local economic conditions that impact the borrower; or
- the value of collateral significantly decreases as a result of deteriorating market conditions.

The carrying amount of the asset is reduced through the use of a provision account and the amount of the loss is recognised in the statement of comprehensive income. The assessment of the evidence for impairment and the determination of the amount of provision for impairment or its reversal require the application of Management's judgment and estimates. Management's judgments and estimates consider relevant factors including, but not limited to, the identification of non-performing loans and high risk loans, the Bank's past loan loss experience, known and inherent risks in the portfolio of loans, adverse situations that affects the borrowers' ability to repay, the estimated value of any underlying collateral and current economic conditions as well as other relevant factors affecting loan and advance recoverability and collateral values. These judgments and estimates are reviewed periodically, and historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. The Management of the Bank has made their best estimates of losses, based on objective evidence of impairment and believes those estimates presented in the financial statements are reasonable in light of available information. Nevertheless, it is reasonably possible, based on existing knowledge, that outcomes within the next financial year that are different from assumptions could require a material adjustment to the carrying amount of the asset or liability affected.

When loans and receivables cannot be recovered, they are written off and charged against provision for loan impairment losses. They are not written off until all the necessary legal procedures have been completed and the amount of the loss is finally determined.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (continued)

**(i) Off-balance sheet commitments**

The Bank enters into off-balance sheet commitments, related to undrawn credit lines, letters of credit and financial guarantees. Financial guarantees represent irrevocable assurances to make payments in the event that a customer cannot meet its obligations to third parties and carry the same credit risk as loans. Financial guarantees and commitments to provide a loan are initially recognised at their fair value, which is normally evidenced by the amount of fees received. This amount is amortised on a straight line basis over the life of commitment, except for commitments to originate loans if it is probable that the Bank will enter into a specific lending arrangement and does not expect to sell the resulting loan shortly after the origination; such loan commitment fees are deferred and included in the carrying value of the loan on initial recognition. At each balance sheet date, the commitments are measured at the higher of (i) the remaining unamortised balance of the amount at initial recognition and (ii) the best estimate of expenditure required settling the commitment at the balance sheet date.

**(j) Financial assets at fair value through profit or loss**

This category has two sub-categories: financial assets held for trading and those designated at fair value through profit or loss at inception. Financial assets at fair value through profit or loss comprise debt securities held by the Bank for trading purposes. They are accounted for at fair value with all gains and losses from revaluation and trading reported in the statement of comprehensive income. Interest earned while holding trading securities is reported as interest income.

All regular way purchases and sales of financial assets held for trading are recognised at trade date, which is the date that the Bank commits to purchase or sell the asset.

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Bank has transferred substantially all risks and rewards of ownership.

**(k) Sale and repurchase agreements of securities**

Sale and repurchase agreements are accounted for as financing transactions. Under sale and repurchase agreements, where the Bank is a transferor, assets transferred remain on the Bank’s balance sheets and are subject to the Bank’s usual accounting policies, with the purchase price received included as a liability owed to the transferee. Where the Bank is a transferee, the assets are not included in the Bank’s balance sheet, but the purchase price paid by it to the transferor is included as an asset. Interest income or expense arising from outstanding sale and repurchase agreements is recognised in the statement of comprehensive income over the term of the agreement using the effective interest method.

**(l) Derivative financial instruments**

Derivative financial instruments include foreign exchange contracts, currency and interest rate swaps held by the Bank for trading purposes. Derivative financial instruments are recognised on trade date and categorised as financial assets at fair value through profit or loss. They are initially recognised in the balance sheet at fair value and subsequently measured at their fair value with all gains and losses from revaluation reported in the profit and loss statement. All derivatives are carried as financial assets when fair value is positive and as financial liabilities when fair value is negative.

**(m) Due from other banks**

Amounts due from other banks are recorded when the Bank advances money to counterparty banks with no intention of trading the resulting unquoted non-derivative receivable due on fixed or determinable dates. Amounts due from other banks are carried at amortised cost.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (continued)

**(n) Available-for-sale financial assets**

Available-for-sale financial assets are comprised of financial instruments held by the Bank for an indefinite period of time which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices. They are stated at fair value with all gains and losses from revaluation recognised in statement of comprehensive income except for foreign exchange gains and losses until derecognition at which time the cumulative gain or loss previously recognised in equity is recognised in the income statement. Dividends on investment securities available-for-sale are recognised in the income statement when the right to receive payment is established.

**(o) Fair values of financial assets and liabilities**

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The best evidence of fair value is price in an active market. An active market is one in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. Fair values of financial assets or liabilities, including derivative financial instruments, in active markets are based on quoted market prices. If the market for a financial asset or liability is not active (and for unlisted securities), the Bank establishes fair value by using valuation techniques. These include the use of discounted cash flow analysis, option pricing models and recent comparative transactions as appropriate, and may require the application of management’s judgment and estimates.

Where, in the opinion of the Management, the fair values of financial assets and liabilities differ materially from their book values, such fair values are separately disclosed in the notes to the accounts.

**(p) Derecognition of financial assets**

The Bank derecognises financial assets when (i) the assets are redeemed or the rights to cash flows from the assets otherwise expired or (ii) the Bank has transferred substantially all the risks and rewards of ownership of the assets or (iii) the Bank has neither transferred nor retained substantially all risks and rewards of ownership but has not retained control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale.

**(q) Intangible assets**

Acquired computer software licences are recognised as intangible assets on the basis of the costs incurred to acquire and bring to use the software. These costs are amortised on the basis of their expected useful lives, not exceeding five years.

**(r) Property and Equipment**

All property and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset’s carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. Such costs are depreciated over the asset's remaining useful life period. All other repairs and maintenance are charged to the statement of comprehensive income during the financial period in which they are incurred.

Depreciation is calculated using the straight-line method to allocate cost of the fixed assets to their residual values over their estimated useful lives, as follows:

| | |
|---|---|
| Building | 50 years |
| Office equipment | 10 years |
| Computers | 3 years |
| Transport | 5 years |

Land is not depreciated. The assets’ residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

Leasehold improvements are capitalised and depreciated over their expected useful lives, or over the remaining lease contract period if shorter, on a straight-line basis.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (continued)

**(r) Property and Equipment** (continued)

Property and equipment are periodically reviewed for impairment. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use.

Gains or losses on disposals are determined by comparing carrying amount with proceeds and are charged to the statement of comprehensive income in the period in which they are incurred.

**(s) Operating lease – the Bank is a lessee**

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any financial incentives received from the lessor) are charged to the statement of comprehensive income on a straight-line basis over the period of the lease.

**(t) Customer accounts**

Customer accounts are non-derivative liabilities to individuals, state or corporate customers and are carried at amortised cost.

**(u) Borrowings**

Borrowings are recognised initially at fair value net of transaction costs incurred. Borrowings are subsequently stated at amortised cost and any difference between net proceeds and the redemption value is recognised in the statement of comprehensive income over the period of the borrowings using the effective interest method.

**(v) Provisions**

Provisions are recognised when the Bank has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made. The assessment of provisions requires the application of management's judgment and estimates, as to the probability of an outflow of resources, the probability of recovery of resources from corresponding sources including security or collateral agreements were appropriate, and the amounts and timings of such outflows, if any.

**(w) Dividends**

Dividends are recorded in equity in the period in which they are declared. Dividends declared after the balance sheet date and before the financial statements are authorised for issue are disclosed in the subsequent events note. The statutory accounting reports of the Bank are the basis for profit distribution and other appropriations. Latvian legislation identifies the basis of distribution as retained earnings.

**(x) Employee benefits**

The Bank pays State compulsory social security contributions for state pension insurance and to the state funded pension scheme in accordance with Latvian legislation. State funded pension scheme is a defined contribution plan under which the Bank pays fixed contributions determined by the law and it will have no legal or constructive obligations to pay further contributions if the state pension insurance system or state funded pension scheme are not able to settle their liabilities to employees. According to the rulings of the Cabinet of Ministers of the Republic of Latvia 69.99% (2015: 71.55%) of the social security contributions are used to finance state funded pension scheme.

Short-term employee benefits, including salaries and state compulsory social security contributions, bonuses and paid vacation benefits, are included in Administrative expenses on an accrual basis.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (continued)

**(y) Off-balance sheet instruments**

In the ordinary course of business, the Bank utilises off-balance sheet financial instruments including commitments to extend loans and advances, financial guarantees and commercial letters of credit. Such financial instruments are recorded in the financial statements when they are funded or related fees are incurred or received. The methodology for provisioning against off-balance sheet instruments is given in paragraph (v) of Note 3 above.

**(z) Trust operations**

Funds managed or held in custody by the Bank on behalf of individuals, trusts and other institutions are not regarded as assets of the Bank and, therefore, are not included in the balance sheet.

Accounting for trust operations is separated from the Bank's own accounting system thus ensuring separate accounting in a separate trust balance sheet for assets of each client, by client and by type of assets under management.

**(aa) Offsetting of Financial Assets and Liabilities**

Financial assets and liabilities are offset and net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

**(bb) Significant Accounting Estimates**

*Loans and advances Assessment*

The Bank regularly assesses the issued loans, whether there has been no loan impairment. In order to determine whether an impairment loss should be recognised in the income statement, the Bank uses estimates and assumptions in respect of the recoverable amount of the loans, including the fair value and cost to sell of the collaterals and the timing of sale of collaterals. The management of the Bank has estimated that provisions recognised based on the individual assessment of the loans are sufficient to cover all impairment losses related to loss events incurred before the balance sheet date. The main indicator of incurrence of loss event is considered to be delays in principal or interest payments. If overdue loans in the loan portfolio would increase by 1%, provisions for loan impairment losses would increase by EUR 350 thousand (2015: EUR 497 thousand).

*Initial recognition of related party transactions*

The Bank is be carrying out transactions with related parties as part of their core business. IAS 39 requires initial recognition of financial instruments at fair value. Cases where the transactions carried out do not have an active market are subject to management judgment in determining interest rates on transactions and their compliance with the market interest rates. Assessment is based on similar types of transactions with unrelated parties and effective interest rate analysis.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (continued)

**(cc) Adoption of new or revised standards and interpretations**

The following new and amended IFRS and interpretations became effective in 2016, but have no significant impact on these financial statements:

Amendments to IFRS 11 “Joint Arrangements” – Accounting for Acquisitions of Interests in Joint Operations (effective for annual periods beginning on or after 1 January 2016).

Amendments to IAS 16 “Property, Plant and Equipment” and IAS 38 “Intangible Assets” - Clarification of Acceptable Methods of Depreciation and Amortisation (effective for annual periods beginning on or after 1 January 2016).

Amendments to IAS 16 “Property, Plant and Equipment” and IAS 41 “Agriculture” – regarding bearer plants (effective for annual periods beginning on or after 1 January 2016).

Amendments to IAS 27 “Separate Financial Statements” - Equity Method in Separate Financial Statements (effective for annual periods beginning on or after 1 January 2016).

Amendments to IAS 1 “Presentation of financial statements” regarding disclosure initiative (effective for annual periods beginning on or after 1 January 2016).

Amendments to IFRS 10 “Consolidated financial statements”, IFRS 12 “Disclosure of Interests in Other Entities” and IAS 28 “Investments in associates and joint ventures” – Investment Entities: Applying the Consolidation Exception (effective for annual periods beginning on or after 1 January 2016).

Annual improvements to IFRS’s 2014 (effective for annual periods beginning on or after 1 January 2016). The amendments include changes that affect 4 standards:

- IFRS 5 “Non-current assets held for sale and discontinued operations”,
- IFRS 7 “Financial instruments: Disclosures” with consequential amendments to IFRS 1,
- IAS 19 “Employee benefits”, and
- IAS 34 “Interim financial reporting”.

Amendments to IAS 19 “Employee benefits plans” regarding defined benefit plans (effective for annual periods beginning on or after 1 February 2015).

Annual improvements to IFRS’s 2012 (effective for annual periods beginning on or after 1 February 2015). These amendments include changes that affect 6 standards:

- IFRS 2 “Share-based payment”,
- IFRS 3 “Business Combinations”,
- IFRS 8 “Operating segments”,
- IAS 16 “Property, plant and equipment” and IAS 38 “Intangible assets”, and
- IAS 24 “Related party disclosures”.

IAS 24 “Disclosures on related party transactions”.

Certain new standards and interpretations have been published that become effective for the annual periods beginning on 1 January 2017 or later periods or are not yet endorsed by the EU and which are relevant to the Bank’s and Group’s operations:

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (continued)

**(cc) Adoption of new or revised standards and interpretations** (continued)

IFRS 9 “Financial instruments” (effective for annual periods beginning on or after 1 January 2018). Key features of the new standard are:

- Financial assets are required to be classified into three measurement categories: those to be measured subsequently at amortised cost, those to be measured subsequently at fair value through other comprehensive income (FVOCI) and those to be measured subsequently at fair value through profit or loss (FVPL).

- Classification for debt instruments is driven by the entity’s business model for managing the financial assets and whether the contractual cash flows represent solely payments of principal and interest (SPPI). If a debt instrument is held to collect, it may be carried at amortised cost if it also meets the SPPI requirement. Debt instruments that meet the SPPI requirement that are held in a portfolio where an entity both holds to collect assets’ cash flows and sells assets may be classified as FVOCI. Financial assets that do not contain cash flows that are SPPI must be measured at FVPL (for example, derivatives). Embedded derivatives are no longer separated from financial assets but will be included in assessing the SPPI condition.

- Investments in equity instruments are always measured at fair value. However, management can make an irrevocable election to present changes in fair value in other comprehensive income, provided the instrument is not held for trading. If the equity instrument is held for trading, changes in fair value are presented in profit or loss.

- Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The key change is that an entity will be required to present the effects of changes in own credit risk of financial liabilities designated at fair value through profit or loss in other comprehensive income.

- IFRS 9 introduces a new model for the recognition of impairment losses – the expected credit losses (ECL) model. There is a ‘three stage’ approach which is based on the change in credit quality of financial assets since initial recognition. In practice, the new rules mean that entities will have to record an immediate loss equal to the 12-month ECL on initial recognition of financial assets that are not credit impaired (or lifetime ECL for trade receivables). Where there has been a significant increase in credit risk, impairment is measured using lifetime ECL rather than 12-month ECL. The model includes operational simplifications for lease and trade receivables.

- Hedge accounting requirements were amended to align accounting more closely with risk management. The standard provides entities with an accounting policy choice between applying the hedge accounting requirements of IFRS 9 and continuing to apply IAS 39 to all hedges because the standard currently does not address accounting for macro hedging.

IFRS 15 “Revenue from Contracts with Customers” (effective for annual periods beginning on or after 1 January 2018);

Amendments to IAS 7 “Statement of Cash Flows” – Disclosure initiative (effective for annual periods beginning on or after 1 January 2017, not yet endorsed in the EU);

IFRS 16 “Leases” (effective for annual periods beginning on or after 1 January 2019, not yet endorsed in the EU);

Amendments to IAS 12 “Income taxes” - recognition of Deferred Tax Assets for Unrealised Losses (effective for annual periods beginning on or after 1 January 2017, not yet endorsed in the EU);

Amendments to IFRS 15 “Revenue from Contracts with Customers” (effective for annual periods beginning on or after 1 January 2018, not yet endorsed in the EU);

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (continued)

**(cc) Adoption of new or revised standards and interpretations** (continued)
Following standards and interpretations are published and are effective for annual periods on or after 1 January 2017 or are not yet endorsed in EU and which management of the Group and Bank consider not relevant for Group's and Bank's operations:

Amendments to IFRS 10 "Consolidated financial statements", IAS 28 "Investments in associates and joint ventures" – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (effective date to be determined by the IASB, not yet endorsed in the EU);

Amendments to IFRS 2 "Share-based Payment" (effective for annual periods beginning on or after 1 January 2018, not yet endorsed in the EU);

Amendments to IFRS 4 "Insurance Contracts" – Applying IFRS 9 "Financial statements" with IFRS 4 "Insurance contracts" (effective for annual periods beginning on or after 1 January 2018, not yet endorsed in the EU);

Annual improvements to IFRS's 2016. The amendments include changes that affect 3 standards:
- IFRS 12 "Disclosure of Interests in Other Entities" (effective for annual periods beginning on or after 1 January 2017, not yet endorsed in the EU),
- IFRS 1 "First-time Adoption of International Financial Reporting Standards" (effective for annual periods beginning on or after 1 January 2018, not yet endorsed in the EU), and
- IAS 28 "Investments in Associates and Joint Ventures" (effective for annual periods beginning on or after 1 January 2018, not yet endorsed in the EU).

IFRIC 22 "Foreign Currency Transactions and Advance Consideration" (effective for annual periods beginning on or after 1 January 2018, not yet endorsed in the EU);

Amendments to IAS 40 "Investment Property" - Transfers (effective for annual periods beginning on or after 1 January 2018, not yet endorsed in the EU).

The Group and the Bank has elected not to adopt these standards, revisions and interpretations in advance of their effective dates. The Group and the Bank anticipates that the adoption of the new standards, revisions and interpretations will have no material impact on the financial statements of the Group and the Bank in the period of initial application, except for IFRS 9, where the impact is being estimated.

**(dd) Categories of financial instruments**
Financial instruments held by the Group and the Bank can be classified as Loans and receivables, Financial assets/ liabilities at fair value through profit or loss, Available-for-sale financial assets and financial liabilities at amortised cost. The Group or Bank do not possess Held to maturity instruments. Financial instruments held by the Group and the Bank and presented on the balance sheet are split by categories as follows:
- Loans and receivables are comprised of Cash and balances with the Bank of Latvia, Balances due from banks, Loans and advances to customers and Other financial assets;
- Financial assets at fair value through profit or loss are comprised of Financial assets at fair value through profit or loss and Derivative financial instruments;
- Available-for-sale financial assets are comprised of Available for sale financial assets;
- Financial liabilities at fair value with revaluation through profit or loss are comprised of Derivative financial instruments;

Financial liabilities at amortised cost are comprised of Balances due to banks, Customer accounts, Subordinated loan, Debt securities and Other financial liabilities.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

## NOTE 4 FINANCIAL RISK MANAGEMENT

**Risk Management**

Risk management is one of the Group's and Bank's strategic tasks. Risk management strategy has been developed for the Bank's risk management, which covers management of the following risks: credit risk, operational risk, market risk, interest rate risk, foreign currency risk, liquidity risk, concentration risk, country risk and other risks.

For the purpose of managing these risks, internal risk management policies and procedures have been developed which are approved by the Bank's Council and/or Board and implemented by the responsible units of the Bank.

The Board of the Bank is responsible for the development and effective functioning of the risk management system and ensuring the identification and management of the Bank's risks, including estimation, evaluation, oversight and preparation of risk reports through implementing the risk identification and management policy set by the Bank's Council and other documents connected with risk management.

Risk Director is responsible for the risk control function in the Bank, oversees the risk management system and co-ordinates actions of all structural units of the Bank related to the risk management. The main unit responsible for determination, evaluation and oversight of the risks is the Risk Management Department, which is an independent unit whose functions are separated from the functions of the business units.

The risk management system is being constantly improved in accordance with the Bank's activities and external conditions influencing these activities. The regular oversight of this process is performed by the Internal Audit Department.

### (a) Credit risk

Credit risk is the risk of incurring losses in the event that a borrower (debtor) or a business partner is unable to fulfil its obligations to the Bank in accordance with the provisions of the contract. Credit risk is present in the Bank's operations where the Bank makes claims against another person and which are reflected in the Bank's balance sheet and off-balance sheet items.

The Bank's principles for evaluation, oversight and acceptance of credit risk are described and approved in its Loan Policy, Business Partner Risk Policy and Investment Portfolio Policy.

The Bank divides up and oversees its credit risk by setting limits of various types and categories: acceptable risk limits for each borrower, group of related borrowers, geographical regions, business sectors, type and value of collateral, currency, term and ratings granted by international agencies. Credit risk exposures are monitored on a revolving basis through regular assessments of borrowers' ability to meet interest and principal maturities and limits are adjusted as appropriate. The Bank's exposure to credit risk is managed and minimised by obtaining collaterals and guarantees against credit exposures that are registered in the name of the Bank. The fair values of those are also reviewed on a regular basis.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 4 FINANCIAL RISK MANAGEMENT** (continued)

**(a) Credit risk** (continued)

The table below shows credit risk exposures relating to on-balance sheet assets and off-balance sheet items before collateral held or other credit enhancements:

| | 31.12.2016 | 31.12.2016 | 31.12.2015 | 31.12.2015 |
|---|---|---|---|---|
| | Grupa | Banka | Grupa | Banka |
| | EUR | EUR | EUR | EUR |
| **Credit risk exposures relating to on-balance sheet assets are as follows:** | | | | |
| Balances on demand with the Bank of Latvia | 147,836,974 | 147,836,974 | 113,537,989 | 113,537,989 |
| Loans to banks | 99,833,647 | 99,833,647 | 142,561,234 | 142,561,234 |
| Loans to customers | 99,513,448 | 99,513,448 | 67,784,042 | 67,784,042 |
| Financial assets at fair value through profit or loss | 125,243,072 | 125,243,072 | 288,969,771 | 288,969,771 |
| Derivative financial instruments | 483,074 | 483,074 | 262,735 | 262,735 |
| Other assets | 3,121,086 | 3,121,049 | 2,775,153 | 2,775,153 |
| **Total** | **476,031,301** | **476,031,264** | **615,628,189** | **615,628,189** |
| **Credit risk exposures relating to off-balance sheet items are as follows:** | | | | |
| Guarantees issued | 5,460,027 | 5,460,027 | 10,725,694 | 10,725,694 |
| Credit related commitments | 20,762,556 | 20,762,556 | 24,536,046 | 24,536,046 |
| **Total** | **26,222,583** | **26,222,583** | **35,261,740** | **35,261,740** |

The Bank regularly reviews the quality of the loan portfolio with the aim to identify loss events. In case loss event is identified, it is assessed whether impairment should be recognised. One of criteria in determining credit quality is overdue days of the payment, as compared to the original agreement date. Credit quality criteria applied to loans from legal entities are results of operating activities of the borrower, as well as perspective for development, current and planned cash flow available for settlement of liabilities, compliance with monitoring/ risk factors, value of collateral etc.

Significantly overdue loans are those overdue for more than 90 days. Impaired loans are loans for which the Bank has raised provisions arising from loss event, as well as loans overdue for more than 90 days and loans where it is planned to begin the process of loan recovery. In these financial statements, information on overdue loans is disclosed starting with the first overdue day.

Loan loss events are:

- Significant financial difficulty of the borrower;
- Breach of loan covenants;
- Relieves provided to the borrower due to such economic or legal aspects that are related to financial difficulties of the borrower, which the Bank would not provide otherwise;
- Rather big probability that borrower will start bankruptcy procedure or any other type of financial reorganisation;
- Not being able to meet the preconditions of the project, underlying the issuance of the loan;
- Breach of liabilities due from borrower’s related party, which has an impact on the ability of the borrower to fulfil his obligations;
- Decrease in value of collateral, in case the repayment of the loan is directly related to the value of collateral;
- Other events increasing credit risk.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 4 FINANCIAL RISK MANAGEMENT** (continued)

**(a) Credit risk** (continued)

The primary factors that the Bank considers in determining whether a loan is impaired are its overdue status and liquidity of related collateral, if any.

The Bank classifies its loans which are not impaired as standard loans, close control loans and substandard loans.

Standard loans are loans, maturity of which is not doubted. Standard loans are those, impairment provisions for which based on present value of future cash flows are 0% to 1%. Standard loans are comprised of loans to legal entities with no expectancy of fulfilment of obligation, as current and future cash flow is sufficient to fulfil the obligations.

Close control loans are loans requiring additional control from the Bank, as these have potential uncertainly, which if remains the same, may potentially endanger fulfilment of obligations in the future and create loss to the Bank. Close control loans are all those loans where impairment provisions calculated based on present value of future cash flows are 1% to 20%. Close control loans are comprised of loans, where:

- Economical or market conditions have adverse impact on the borrower or his industry;
- Tendencies of deterioration of financial position of the borrower are observed or the balance sheet of the borrower is indicative of instability, however, not that significant, as to endanger the repayment of the loan at present.

Substandard loans are loans with clear uncertainties about the fulfilment of credit obligations in full amount and which will create loss to the Bank, if the uncertainty is not removed. Substandard loans are all those loans where impairment provisions calculated based on present value of future cash flows are above 21%. Loans classified as substandard are comprised of loans, where:

- Cash flows of the borrower are insufficient to ensure regular payments are made in accordance with the agreement terms;
- The Bank received insufficient current information about financial condition of the borrower or inappropriate documentation on the conditions of the pledge and sources of fulfilment of credit obligations.

**(b) Market risk**

The Bank takes on exposure to market risks. Market risks arise from open positions in interest rate and currency, all of which are exposed to general and specific market movements.

The Bank manages market risks by diversification of financial instruments portfolio, limits set for different types of financial instruments and application of sensitivity tests which show the impact of particular risks on the Bank’s assets and equity.

**(c) Currency risk**

The Bank is exposed to the risk of changing foreign currency exchange rates, which impacts both the financial performance and the cash flows of the Bank. The Bank controls assets and liabilities denominated in foreign currencies to avoid unreasonable foreign currency exchange rate risk. Currency risk is calculated for each currency separately taking into account the amount of liabilities and requirements of the Bank. The Board determines the Bank's open position limits for certain currencies, which are monitored daily. The Latvian banking legislation requires that open positions in each foreign currency may not exceed 10% of the Bank’s equity and that the total foreign currency open position may not exceed 20% of the equity. During 2016 and 2015 the Bank was in compliance with those limits (see Note 25). Bank has no significant open positions in "exotic" currencies.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 4 FINANCIAL RISK MANAGEMENT** (continued)

**(c) Currency risk** (continued)

The Bank’s foreign currency risk evaluation is based on the following main principles:
- evaluation is made of changes to the Bank’s assets, liabilities and off-balance sheet items as a result of exchange rate fluctuations;
- how the Bank’s revenue/costs change with exchange rate fluctuations;
- performance of currency risk stress tests.

The main elements of currency risk management:
- currency risk evaluation;
- setting of limits and restrictions;
- monitoring of adherence to internal limits;
- performance of exchange rate stress tests and analysis of obtained results;
- entering into hedging relationships if necessary.

The Bank defines and controls daily and weekly maximum loss limits, via involving in currency trading.

As part of a quarterly currency risk management process, assessment of the foreign exchange risk is performed (it is assessed how the balance sheet and off-balance sheet items change with the changes in foreign currency exchange rates, how the income/expenses of the Bank change with the foreign currency exchange rate changes) and the results of such evaluation are submitted to the Bank's management. Once a year a currency risk stress testing and the analysis of its results is performed, on the basis of which proposals for changes to the Foreign currency risk management policy are made to the management of the Bank, if necessary.

The following table shows the sensitivity of profit/ loss to currency exchange rate fluctuations at the end of the reporting period, with other conditions constant (in thousand EUR):

| **31.12.2016** | **Effect on profit/ loss and equity** | | **31.12.2015** | **Effect on profit/ loss and equity** | |
|---|---|---|---|---|---|
| | **+10%** | **-10%** | | **+10%** | **-10%** |
| **USD** | (30) | 30 | **USD** | (50) | 50 |
| **Total** | **(30)** | **30** | **Total** | **(50)** | **50** |

**(d) Interest rate risk**

Interest rate risk is the sensitivity of the financial position of the Bank to a change in market interest rates. In the normal course of business, the Bank encounters interest rate risk as a result of differences within maturities or interest re-fixing dates of respective interest-sensitive assets and liabilities. The risk is controlled by the Bank’s Asset and Liability Committee, which sets limits on the level of mismatch of interest rate reprising and evaluates interest rate risk undertaken by the Bank (see Note 30).

The main elements of interest rate risk management:
- evaluation of interest rate risk sensitivity;
- setting of internal limits (limit of reduction in economic value and for total duration of securities portfolio);
- monitoring of adherence to internal limits;
- performance of interest rate stress tests and analysis of obtained results;
- entering into hedging relationships if necessary.

Interest rate risk identification and assessment is made in such a way as to further examine all types of interest-rate risks. To limit the interest rate risk, limits are set for both impairment of economic value, as well as the modified duration of securities portfolio.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 4 FINANCIAL RISK MANAGEMENT** (continued)

**(d) Interest rate risk** (continued)
As part of interest rate risk assessment impact of interest rate changes on the economic value of the Bank is performed regularly, including interest rate risk assessment from income perspective and interest rate risk assessment from the perspective of economic value, and on that basis, follow up control of limits set is carried out. Moreover, interest rate risk stress testing is performed, based on which changes to the interest rate risk management policies are proposed, if needed. Results of interest rate risk assessment are reported to the Bank's management.

Split of the assets/ liabilities/ off-balance sheet items into maturity groups is made on the basis of:
- shorter from the remaining repayment/ settlement/ maturity term – for financial instruments with fixed interest rate;
- for a period until the next interest rate change date or interest repricing date – for financial instruments with variable interest rate.
- maturity of deposits is shown as being not longer than five years.

Assets/ liabilities/ off-balance sheet items with no specified maturity are split into maturity groups as follows:
Settlement accounts, for which interest is paid, are classified as sensitive to the changes in interest rates and presented as “on demand”.

Derivatives are presented as both long off-balance-sheet position and short off-balance-sheet position.

The following changes in interest rates are applied to the sensitivity analysis: all items except for deposits are subject to rate changes of +/-100 base points, while deposits are subject to rate changes of +/-50 base points.

The following table shows the sensitivity of revenue and equity to interest rate fluctuations as described above with other conditions constant (in thousand EUR):

| **31.12.2016** | **Effect on profit/ loss and equity** | | **31.12.2015** | **Effect on profit/ loss and equity** | |
|---|---|---|---|---|---|
| **USD** | (852) | 852 | **USD** | (547) | 547 |
| **EUR** | (166) | 166 | **EUR** | (54) | 54 |
| **Total** | **(1 018)** | **1 018** | **Total** | **(601)** | **601** |

**(e) Liquidity risk**
The Bank is exposed to daily calls on its available cash resources from short-term liquid investments. The relationship between the maturity of assets and liabilities, as well as off-balance sheet items is indicative of liquidity risk and the extent to which it may be necessary to raise funds to meet outstanding obligations.

The Bank does not maintain cash resources to meet all of these needs, as experience shows that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty. The Board sets limits on the minimum proportion of maturing funds available to meet such calls and on the minimum level of inter-bank and other borrowing facilities that should be in place to cover withdrawals at unexpected levels of demand.

It is unusual for banks to be completely matched, as transacted business is often of uncertain term and of different types (see Note 29). An unmatched position potentially enhances profitability, but also increases the risk of losses.

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature are important factors in assessing the liquidity of the Bank and its exposure to changes in interest rates and exchange rates.

The matching and controlled mismatching of the maturities of assets and liabilities is fundamental to the daily liquidity management of the Bank.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 4 FINANCIAL RISK MANAGEMENT** (continued)

**(e) Liquidity risk** (continued)
The Bank uses the following methods for evaluation of liquidity risk:
- preparation of maturity analysis (for all currencies and separately for individual currencies);
- calculation of the liquidity ratio, monitoring of adherence to liquidity ratio regulations;
- stress testing.

The following are the main elements of liquidity risk management:
- being in compliance with liquidity ratio regulations;
- setting of the liquidity net position limit;
- setting of restriction for attracting deposits;
- monitoring of adherence to liquidity limits;
- conducting liquidity stress tests and analysis of results obtained;
- recommendations for resolving liquidity problems.

In accordance with FCMC requirements, the Bank maintains sufficient liquid assets to meet its liabilities in the amount which is not less than 60% of the Bank’s current liabilities.

**(f) Capital adequacy**

Capital adequacy refers to the sufficiency of the Bank’s capital resources to cover risks resulting from the Bank’s operating activities.

In order to calculate the capital for risks to which minimal capital requirements are set, according to the Financial and Capital Market Commission’s (FCMC) regulations on preparation of report on minimal capital requirements, capital requirements are calculated using the following approaches and methods:
-the capital requirements for the credit risk are calculated using the standardised approach,
-“simple method of financial security” is used in order to decrease the credit risk,
-the capital requirements for the foreign exchange risks, capital requirements for the commodities risk, capital requirements for the position risk of debt securities and equities are calculated using the standardised approach,
-the capital requirements for the general risk of debt securities are calculated using maturity method;
-the capital requirements for the operational risk are calculated using the basic index approach.

The Bank also evaluates whether compliance with the minimal capital requirements ensures that the capital of the Bank is sufficient to cover all possible losses associated with all of the above mentioned risks.
Moreover, the Bank has developed internal documentation and regulations according to which it determines the amount of necessary capital for substantial risks to which minimal capital requirements are not set (e.g., interest rates risk, liquidity risk, country risk, and other substantial risks).

Calculated in accordance with the FCMC requirements, the Bank’s capital adequacy ratio as at 31 December 2016 was 30.51 % (as at 31 December 2015 23.26 %), which is above the minimum set by the European Parliament and Council Regula (EU) no. 575/2013 requiring capital retention reserve amount (10.5%), being a sum of equity against risk weighted assets and off-balance sheet items being minimum of 8% and capital retention reserve above 2.5% (see Note 27). At the end of 2016 the Finance and Capital Markets Commission recalculated individual capital adequacy requirements placed on the Bank and determined it to be 13.7%. The Bank observed and complied with the individually determined capital adequacy requirements both as at 31 December 2016 and 31 December 2015.

**(g) Operational risk**
Operational risk is the possibility of incurring losses as a result of inadequate or unsuccessful developments in the Bank’s internal processes, human and systemic actions, or influence of external conditions. Operational risk is defined as the risk of a reduction in the Bank’s revenue/ incurring of additional costs (and a resulting reduction of the equity) due to erroneous transactions with customers/business partners, information processing, adoption of ineffective decisions, insufficient human resources or insufficient planning for the influence of external conditions.

The Bank has established and maintains an Operational Risk Event and Loss database in which internal data on operational risk events and associated losses are collected, processed and organised.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 4 FINANCIAL RISK MANAGEMENT** (continued)

**(g) Operational risk** (continued)

The main elements of operational risk management are:
- operational risk monitoring;
- operational risk control and minimisation:
  - development of internal regulatory documents which prevent/reduce the likelihood of operational events;
  - segregation of duties;
  - control over internal limits;
  - adherence to the procedures in the use of IT and other Bank's resources;
  - appropriate training of employees;
  - regular review of supporting documents for transactions and account balances.

**(h) Concentration risk**

*Transaction concentration risk* is each and every risk deal or group of risk deals that could cause Bank to suffer such losses that may endanger the liquidity of the Bank or its ability to continue on a going concern. Concentration risk arises from significant risk deals with Clients or Group of inter-related Clients or risk deals with Clients with common risk factors (e.g., economy sector, geographical region, currency, instrument used for decrease of credit risk (one type of collateral or one provider of collateral, etc.).

In order to control transaction concentration risk Bank has set limits for investments into various types of assets, instruments, markets, etc. Limit is a numerical threshold applied to various types of investments serving as an instrument for limiting and controlling the risk.

*Country risk* is one of significant transaction concentration risks. Country risk – country partner risk – is the possibility of incurring losses if the Bank's assets are located in a country where, due to changes in its economic and political factors, the Bank may experience problems in recovering its assets within the agreed time and amount. The reasons of default by partners and issuers are primarily currency devaluation, unfavourable legislative changes, creation of new restrictions and barriers as well as other, including force majeure, factors.

In order to control concentration risks following limits were set:
- currency risk limits;
- credit rating group limits;
- financial market operations risk limits;
- limits on open currency positions and cash, limits on allowable loss on trading with foreign currencies;
- limits on allowable loss from trading with financial instruments portfolios;
- limits on high risk deals;
- limits on transactions with parent bank;
- limits on crediting programmes.

Control, analysis and review of fulfilment of these limits is performed.

International rating organisations data (including credit ratings and their dynamics), economic indicators of the country and other relevant information is used for risk analysis.

The main elements of risk control:
- setting of internal limits for regions, countries, and by transaction types in individual countries;
- monitoring of adherence to internal limits;
- analysis and monitoring of country risk;
- review of internal limits.

Asset, liability and off-balance sheet country risk applies to the country which is considered to be the primary country where the client conducts its business activities. If a loan is granted to a resident of another country using collateral which is physically located in a country other than the resident country of the legal entity, the state risk is transferred to the country where the loan collateral is actually located.

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### NOTE 5 INTEREST INCOME AND EXPENSE

| | 2016 | 2016 | 2015 | 2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| **Interest income** | | | | |
| Loans and advances to legal entities | 5,631,576 | 5,631,576 | 4,798,204 | 4,798,204 |
| Loans and advances to private individuals | 710,730 | 710,730 | 133,089 | 133,089 |
| Balances due from banks | 1,653,308 | 1,653,308 | 2,040,044 | 2,040,044 |
| Trading securities | 1,587,689 | 1,587,689 | 1,322,193 | 1,322,193 |
| **Total interest income** | **9,583,303** | **9,583,303** | **8,293,530** | **8,293,530** |
| **Interest expense** | | | | |
| Due to private individuals | (139,513) | (139,513) | (679,048) | (679,048) |
| Due to legal entities | (1,844,292) | (1,844,292) | (2,202,066) | (2,202,066) |
| Subordinated loan | (1,072,180) | (1,072,180) | (1,067,257) | (1,067,257) |
| Debt securities issued | (433,362) | (433,362) | - | - |
| Other interest and related expenses | (1,008,404) | (1,008,404) | (1,441,611) | (1,441,611) |
| **Total interest expense** | **(4,497,751)** | **(4,497,751)** | **(5,389,982)** | **(5,389,982)** |
| **Net interest income** | **5,085,552** | **5,085,552** | **2,903,548** | **2,903,548** |

Interest income from impaired loans amounts to 1,157,255 EUR (2015: 1,754,748 EUR).

Other interest and related expenses include payments to the deposit guarantee fund EUR 280,415 (2015: 749,625 EUR), as well as payments to finance the FCMC EUR 115,573 (2015: 127,356 EUR), the financial stability fee of EUR 145,350 (2015: 359,539 EUR) and negative interest rate applied on correspondent accounts of EUR 467,066 (2015: 205,091 EUR).

### NOTE 6 FEE AND COMMISSION INCOME AND EXPENSE

| | 2016 | 2016 | 2015 | 2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| **Fee and commission income** | | | | |
| Money transfers | 5,656,501 | 5,656,558 | 6,644,243 | 6,644,243 |
| Fees on registration of changes in loan agreements | 2,525 | 2,525 | 1,871 | 1,871 |
| Commission income from asset management | 234,864 | 234,864 | 168,445 | 168,445 |
| Accounts servicing | 1,103,548 | 1,103,548 | 945,970 | 945,970 |
| Commissions from letters of credit | 533,062 | 533,062 | 454,142 | 454,142 |
| Commission income on transactions with securities | 114,530 | 114,530 | 53,098 | 53,098 |
| Commission income on current accounts servicing | 134,707 | 134,707 | 136,938 | 136,938 |
| Income from general services | 83,826 | 83,826 | 63,978 | 63,978 |
| Other commissions (DIGIPAS) | 70,144 | 70,144 | 102,570 | 102,570 |
| Interbank commission income | 334,589 | 334,589 | 277,096 | 277,096 |
| Commission for dealing with cards | 279,753 | 279,753 | 231,309 | 231,309 |
| Income from currency exchange | 461,425 | 461,425 | 354,410 | 354,410 |
| Other income | 347,268 | 347,268 | 256,281 | 256,281 |
| **Total fee and commission income** | **9,356,742** | **9,356,799** | **9,690,351** | **9,690,351** |
| **Fee and commission expense** | | | | |
| Money transfers | (1,279,484) | (1,279,484) | (1,442,671) | (1,442,671) |
| Other expense | (39,327) | (39,327) | (41,154) | (41,154) |
| **Total fee and commission expense** | **(1,318,811)** | **(1,318,811)** | **(1,483,825)** | **(1,483,825)** |
| **Net fee and commission income** | **8,037,931** | **8,037,988** | **8,206,526** | **8,206,526** |

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

## NOTE 7 ADMINISTRATIVE EXPENSE

| | 2016 | 2016 | 2015 | 2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| Remuneration paid to personnel | 4,026,460 | 4,023,336 | 3,277,413 | 3,277,413 |
| Rent expense | 62,693 | 62,693 | 130,363 | 130,363 |
| Office and equipment maintenance | 72,996 | 72,996 | 39,269 | 39,269 |
| Remuneration paid to the members of the Council and the Board | 587,076 | 587,076 | 446,486 | 446,486 |
| Security services | 1,810 | 1,810 | 2,100 | 2,100 |
| Public utilities | 126,395 | 126,395 | 101,301 | 101,301 |
| State compulsory social insurance contributions | 1,097,894 | 1,097,158 | 849,280 | 849,280 |
| Communication expense | 514,020 | 514,020 | 404,178 | 404,178 |
| Consulting and professional fees | 965,801 | 949,376 | 223,270 | 223,270 |
| Set-up and maintenance costs of information systems | 201,367 | 201,367 | 161,279 | 161,279 |
| Business trips | 119,821 | 119,821 | 89,393 | 89,393 |
| Credit card expenses | 34,011 | 34,011 | 38,624 | 38,624 |
| Transportation | 40,726 | 40,726 | 40,239 | 40,239 |
| Remuneration of the certified auditor | 36,960 | 36,960 | 36,860 | 36,860 |
| Health insurance | 9,842 | 9,842 | 17,254 | 17,254 |
| Advertising and marketing | 10,000 | 10,000 | - | - |
| Other administrative expense | 761,937 | 761,937 | 589,267 | 589,267 |
| | **8,669,809** | **8,649,524** | **6,446,576** | **6,446,576** |

The average number of staff employed by the Bank in 2016 was 199, including 4 Members of the Board, 5 Members of the Council and 190 other employees (in 2015: 159, including 4 members of the Board, 5 Members of the Council and 150 other employees).

## NOTE 8 OTHER OPERATING INCOME

| | 2016 | 2016 | 2015 | 2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| **Other operating income** | | | | |
| Rent | 385,887 | 385,887 | 261,877 | 261,877 |
| Penalties | 32,505 | 32,505 | 9,333 | 9,333 |
| Other income | 64,066 | 64,066 | 4,620 | 4,620 |
| **Total other operating income** | **482,458** | **482,458** | **275,830** | **275,830** |

## NOTE 9 INCOME TAX EXPENSE

| | 2016 | 2016 | 2015 | 2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| Corporate income tax for the reporting year | 561,487 | 561,487 | - | - |
| Amount of tax paid abroad | 247,747 | 247,747 | 285,021 | 285,021 |
| Deferred tax (see Note 23) | 197,208 | 197,208 | 52,872 | 52,872 |
| **Total corporate income tax** | **1,006,442** | **1,006,442** | **337,893** | **337,893** |

Corporate income tax differs from the theoretically calculated taxation at the 15% rate as stipulated by the law (see below):

| | 2016 | 2016 | 2015 | 2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| **Profit/ (loss) before income tax** | **3,564,255** | **3,584,597** | **(1,231,914)** | **(1,231,914)** |
| Theoretically calculated tax at a tax rate of 15% | 534,638 | 537,690 | (184,787) | (184,787) |
| Loss from revaluation of securities at fair value through profit or loss | 17,211 | 17,211 | 41,201 | 41,201 |
| Other expenses not deductible for tax purposes | 680,023 | 680,023 | 502,426 | 502,426 |
| Non-taxable income and tax allowances | (473,177) | (476,229) | (305,969) | (305,969) |
| Amount of tax paid abroad* | 247,747 | 247,747 | 285,021 | 285,021 |
| **Corporate income tax expense** | **1,006,442** | **1,006,442** | **337,893** | **337,893** |

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

## NOTE 9 INCOME TAX EXPENSE (continued)

* Amount of tax paid abroad is comprised of withholding tax paid in Ukraine. Corporate income tax calculated in Latvia can be reduced by the amount of tax paid abroad, if the payment is certified by the documents approved by the foreign tax authority, indicating the amount of taxable income and the amount of tax withheld abroad. Tax can be reduced by the amount of tax withheld abroad, however, limited to the amount, which would be payable in Latvia for the amount of revenue generated abroad. Amounts of withholding tax, exceeding the tax calculated in Latvia, cannot be carried forward to the future periods, therefore, are recognized as tax expenses in the current period.

## NOTE 10 CASH AND BALANCES WITH THE BANK OF LATVIA

| | 31.12.2016 | 31.12.2016 | 31.12.2015 | 31.12.2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| Cash | 1,069,836 | 1,069,836 | 909,526 | 909,526 |
| Balances on demand with the Bank of Latvia | 147,836,974 | 147,836,974 | 113,537,989 | 113,537,989 |
| | **148,906,810** | **148,906,810** | **114,447,515** | **114,447,515** |

Balances on demand with Bank of Latvia reflect the balance of the Bank's correspondent account, on which interest is paid in the amount of the compulsory reserve requirement.

Demand deposits with the Bank of Latvia include reserves, which are held in accordance with the Regulations of the Bank of Latvia. These Regulations prescribe the minimum level of the Bank's average correspondent account balance per month, while at any given day these monetary means in the account can be freely accessed and used by the Bank.

The minimum level of the Bank's correspondent account for the period from 14 December 2016 to 31 December 2016 was set at EUR 4,021,348 (in 2015: 5,768,172 EUR). The Bank was in compliance with the reserve requirement of the Bank of Latvia during 2016 and 2015.

## NOTE 11 BALANCES DUE FROM BANKS

| | 31.12.2016 | 31.12.2016 | 31.12.2015 | 31.12.2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| Due from Republic of Latvia credit institutions | 22,713,344 | 22,713,344 | 21,468,113 | 21,468,113 |
| Due from non-OECD credit institutions | 36,852,154 | 36,852,154 | 52,218,409 | 52,218,409 |
| Due from OECD credit institutions | 40,366,032 | 40,366,032 | 68,972,595 | 68,972,595 |
| **Balances due from banks, gross** | 99,931,530 | 99,931,530 | **142,659,117** | **142,659,117** |
| Provisions for impairment of balances due from banks | (97,883) | (97,883) | (97,883) | (97,883) |
| **Balances due from banks, net** | **99,833,647** | **99,833,647** | **142,561,234** | **142,561,234** |

As at 31 December 2016 Balances due from banks included receivables amounting to 97,883 EUR from Zlatobank, which informed the Bank on the suspension of its operations. The Bank has created provisions amounting to 100% of these receivables. Other balances due from banks are not overdue and are not impaired. Balances due from banks are not collateralised.

The following table discloses balances due from banks based on their type:

| | 31.12.2016 | 31.12.2016 | 31.12.2015 | 31.12.2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| On demand | 75,764,685 | 75,764,685 | 98,648,930 | 98,648,930 |
| Balances with maturity of three months or less | 20,061,070 | 20,061,070 | 31,003,841 | 31,003,841 |
| Other balances due from banks | 4,105,775 | 4,105,775 | 13,006,346 | 13,006,346 |
| **Balances due from banks, gross** | 99,931,530 | 99,931,530 | **142,659,117** | **142,659,117** |
| Provisions for impairment of balances due from banks | (97,883) | (97,883) | (97,883) | (97,883) |
| **Balances due from banks, net** | **99,833,647** | **99,833,647** | **142,561,234** | **142,561,234** |

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 11 BALANCES DUE FROM BANKS** (continued)

The following table discloses Group's and Bank's balances due from banks according to their ratings as at 31 December 2016 and 31 December 2015:

| | 31.12.2016. | | 31.12.2015. | |
|---|---|---|---|---|
| **Rating** | **Due from banks EUR** | **%** | **Due from banks EUR** | **%** |
| Aaa to Aa3 | 33,005 | 0.03% | - | - |
| A1 to A3 | 4,911,581 | 4.91% | 20,184,373 | 14.16% |
| Baa1 to Baa3 | 33,493,460 | 33,53% | 61,109,415 | 42,87% |
| Ba1 to Ba3 | 7,138,005 | 7.14% | 500,440 | 0.35% |
| B1 to B3 | 11,690,941 | 11.70% | 14,700,488 | 10.31% |
| Below B3 | 18,678,484 | 18.69% | 23,252,019 | 16.31% |
| | **75,945,476** | **76.00%** | **119,746,735** | **84.00%** |
| **Without rating** | 23,986,054 | 24.00% | 22,912,382 | 16.00% |
| Provisions for impairment of balances due from banks | (97,883) | - | (97,883) | - |
| **Balances due from banks, net** | **99,833,647** | **100.00%** | **142,561,234** | **100.00%** |

**NOTE 12 LOANS AND ADVANCES TO CUSTOMERS**

Analysis of loans by client type and by products:

| | 31.12.2016 | 31.12.2016 | 31.12.2015 | 31.12.2015 |
|---|---|---|---|---|
| | **Group** | **Bank** | **Group** | **Bank** |
| | **EUR** | **EUR** | **EUR** | **EUR** |
| Loans to legal entities | 122,280,132 | 122,280,132 | 100,341,556 | 100,341,556 |
| Loans to private individuals, except for mortgages | 10,175,017 | 10,175,017 | 1,676,857 | 1,676,857 |
| Mortgages | 2,066,285 | 2,066,285 | 1,956,288 | 1,956,288 |
| **Gross loans and advances to customers** | **134,521,434** | **134,521,434** | **103,974,701** | **103,974,701** |
| Less: provisions for loan impairment | (35,007,986) | (35,007,986) | (36,190,659) | (36,190,659) |
| **Total loans and advances to customers** | **99,513,448** | **99,513,448** | **67,784,042** | **67,784,042** |

The following table discloses changes in Group's and Bank's provisions for loan impairment during 2016:

| | Loans to legal entities EUR | Loans to private individuals, except for mortgages EUR | Mortgages EUR | Total EUR |
|---|---|---|---|---|
| **Provisions for loan impairment as at 1 January 2016** | **33,154,537** | **1,634,060** | **1,402,062** | **36,190,659** |
| Increase in provisions for loan impairment for the year | 5,324,455 | (2,378) | (15) | 5,322,062 |
| Write-off of loans | (7,232,345) | (164) | - | (7,232,509) |
| Impact of foreign currency revaluation | 692,364 | - | 35,410 | 727,774 |
| **Provisions for loan impairment as at 31 December 2016** | **31,939,011** | **1,631,518** | **1,437,457** | **35,007,986** |

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 12 LOANS AND ADVANCES TO CUSTOMERS** (continued)

The following table discloses changes in provisions for Group's and Bank's loan impairment during 2015:

| | Loans to legal entities | Loans to private individuals, except for mortgages | Mortgages | Total |
|---|---|---|---|---|
| | EUR | EUR | EUR | EUR |
| **Provisions for loan impairment as at 1 January 2015** | **26,076,601** | **1,629,049** | **1,291,482** | **28,997,132** |
| Increase in provisions for loan impairment for the year | 7,910,113 | 5,627 | (928) | 7,914,812 |
| Write-off of loans | (2,935,051) | (616) | - | (2,935,667) |
| Impact of foreign currency revaluation | 2,102,874 | - | 111,508 | 2,214,382 |
| **Provisions for loan impairment as at 31 December 2015** | **33,154,537** | **1,634,060** | **1,402,062** | **36,190,659** |

The concentration of risks in the credit portfolio based on the economical industries is as follows:

| | 31.12.2016 Group | | 31.12.2016 Bank | | 31.12.2015 Group | | 31.12.2015 Bank | |
|---|---|---|---|---|---|---|---|---|
| | EUR | % | EUR | % | EUR | % | EUR | % |
| Trade and commercial activities | 27,469,209 | 20.42 | 27,469,209 | 20.42 | 32,314,677 | 31.08 | 32,314,677 | 31.08 |
| Private individuals | 12,241,303 | 9.10 | 12,241,303 | 9.10 | 3,633,145 | 3.49 | 3,633,145 | 3.49 |
| Agriculture and food industry | 6,228,047 | 4.63 | 6,228,047 | 4.63 | 2,729,191 | 2.62 | 2,729,191 | 2.62 |
| Construction and operations with real estate | 25,370,363 | 18.86 | 25,370,363 | 18.86 | 28,098,792 | 27.02 | 28,098,792 | 27.02 |
| Transport and communication | 38,601,255 | 28.70 | 38,601,255 | 28.70 | 15,143,291 | 14.56 | 15,143,291 | 14.56 |
| Industry | 10,522,899 | 7.82 | 10,522,899 | 7.82 | 10,651,285 | 10.24 | 10,651,285 | 10.24 |
| Tourism and hotel services, restaurant business | 2,017,050 | 1.50 | 2,017,050 | 1.50 | 155,318 | 0.15 | 155,318 | 0.15 |
| Financial services | 3,607,029 | 2.68 | 3,607,029 | 2.68 | 4 066 598 | 3.91 | 4 066 598 | 3.91 |
| Other | 8,464,281 | 6.29 | 8,464,281 | 6.29 | 7,182,404 | 6.91 | 7,182,404 | 6.91 |
| **Loans and advances to customers (before provisions for impairment)** | **134,521,436** | **100%** | **134,521,436** | **100%** | **103,974,701** | **100%** | **103,974,701** | **100%** |

As at 31 December 2016, the total amount of loans issued to 10 largest customers was EUR 71,316,278 (2015: EUR 45,880,708), which comprises 53.01 % of the total credit portfolio (2015: 44.13 %).

As at 31 December 2016 loans to 10 largest customers were secured by deposits amounting to EUR 8,591,871 EUR (31 December 2015: EUR 13,001,878).

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**12 LOANS AND ADVANCES TO CUSTOMERS** (continued)

Since on 31 December 2016 Bank's subsidiary does not have loans issued to nor received collaterals, the following table shows the information about collateral as at 31 December 2016:

| | Loans to legal entities | Loans to private individuals, except for mortgages | Mortgages | Total |
|---|---|---|---|---|
| | EUR | EUR | EUR | EUR |
| Unsecured | 13,887,684 | 1,723,315 | 677,840 | 16,288,839 |
| Loans with sufficient collateral: | | | | |
| - residential real estate | 846,532 | 54,049 | 507,708 | 1,408,289 |
| - other real estate | 54,623,775 | 8,394,842 | - | 63,018,617 |
| - cash deposits | 5,829,457 | - | - | 5,829,457 |
| - securities | - | - | - | - |
| - guarantees and other assets | 8,247,974 | 2,811 | - | 8 250 785 |
| Loans with insufficient collateral: | | | | |
| - residential real estate | 864,279 | - | - | 864,279 |
| - other real estate | 29,817,171 | - | 880,737 | 30,697,908 |
| - deposits | 2,800,569 | - | - | 2,800,569 |
| - securities | 848,224 | - | - | 848,224 |
| - guarantees and other assets | 4,514,467 | - | - | 4,514,467 |
| **Total loans and advances to customers (before provisions for impairment)** | **122,280,132** | **10,175,017** | **2,066,285** | **134,521,434** |

The following table shows the information about collateral as at 31 December 2015:

| | Loans to legal entities | Loans to private individuals, except for mortgages | Mortgages | Total |
|---|---|---|---|---|
| | EUR | EUR | EUR | EUR |
| Unsecured | 17,639,221 | 1,668,270 | 323,292 | 19,630,782 |
| Loans with sufficient collateral: | | | | |
| - residential real estate | 750,329 | - | 434,363 | 1,184,692 |
| - other real estate | 20,500,324 | - | - | 20,500,324 |
| - cash deposits | 145,788 | 2,902 | - | 148,690 |
| - securities | 245,418 | - | - | 245,418 |
| - guarantees and other assets | 10,511,502 | 4,766 | - | 10,516,269 |
| Loans with insufficient collateral: | | | | |
| - residential real estate | 996,650 | - | 205,742 | 1,202,392 |
| - other real estate | 34,026,612 | - | 992,891 | 35,019,503 |
| - deposits | 13,001,878 | 919 | - | 13,002,797 |
| - guarantees and other assets | 2,523,834 | - | - | 2,523,834 |
| **Total loans and advances to customers (before provisions for impairment)** | **100,341,556** | **1,676,857** | **1,956,288** | **103,974,701** |

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 12 LOANS AND ADVANCES TO CUSTOMERS** (continued)

Since on 31 December 2016 Bank’s subsidiary does not have loans issued to nor received collaterals, the following table shows the loans outstanding as at 31 December 2016 by credit quality:

| | **Loans to legal entities** | **Loans to private individuals, except for mortgages** | **Mortgages** | **Total** |
|---|---|---|---|---|
| | **EUR** | **EUR** | **EUR** | **EUR** |
| *Loans that are neither past due nor impaired* | | | | |
| - Standard loans | 64,766,285 | 8,506,605 | 507,708 | **73,780,598** |
| - Close control | - | - | - | **-** |
| - Substandard | - | - | - | **-** |
| **Total neither past due nor impaired** | **64,766,285** | **8,506,605** | **507,708** | **73,780,598** |
| *Past due but not impaired loans* | | | | |
| - past due up to 30 days | 7,873,989 | - | - | **7,873,989** |
| - past due from 30 to 90 days | - | 36,741 | - | **36,741** |
| - past due from 91 to 180 days | - | 135 | - | **135** |
| - past due from 181 to 360 days | 30 | 5 | - | **35** |
| - past due over 360 days | 50 | 13 | - | **63** |
| **Total past due, but not impaired** | **7,874,069** | **36,894** | **-** | **7,910,963** |
| *Individually impaired loans (total amount)* | | | | |
| - not past due | 20,854,363 | - | - | **20,854,363** |
| - past due up to 30 days | 3,004,089 | - | 1,235,300 | **4,239,389** |
| - past due from 30 to 90 days | 110,205 | - | - | **110,205** |
| - past due 91 – 180 days | 210,803 | - | - | **210,803** |
| - past due 181 – 360 days | - | - | - | **-** |
| - past due over 360 days | 25,460,318 | 1,631,518 | 323,277 | **27,415,113** |
| **Total individually impaired loans (total amount)** | **49,639,778** | **1,631,518** | **1,558,577** | **52,829,873** |
| **Provisions for loan impairment** | **(31,939,011)** | **(1,631,518)** | **(1,437,457)** | **(35,007,986)** |
| **Net loans and advances to customers** | **90,341,121** | **8,543,499** | **628,828** | **99,513,448** |

Loans past due, but not impaired include all amounts due from borrowers. Amount actually overdue as at 31 December 2016 was 324,526 EUR (as at 31 December 2015: 21,881 EUR).

Loans past due and individually impaired include all amounts due from borrowers. Amount actually overdue as at 31 December 2016 was 27,293,924 EUR (as at 31 December 2015: 30,678,925 EUR).

## NOTES TO THE FINANCIAL STATEMENTS (continued)

## NOTE 12 LOANS AND ADVANCES TO CUSTOMERS (continued)

The following table shows the loans outstanding as at 31 December 2015 by credit quality:

| | Loans to legal entities EUR | Loans to private individuals, except for mortgages EUR | Mortgages EUR | Total EUR |
|---|---|---|---|---|
| *Loans that are neither past due nor impaired* | | | | |
| - Standard loans | 42,087,067 | 42,641 | 434,363 | **42,564,071** |
| - Close control | - | - | - | **-** |
| - Substandard | - | - | - | **-** |
| **Total neither past due nor impaired** | **42,087,067** | **42,641** | **434,363** | **42,564,071** |
| *Past due but not impaired* | | | | |
| - past due from 30 to 90 days | 306,285 | 138 | - | **306,423** |
| - past due from 91 to 180 days | 39,097 | - | - | **39,097** |
| - past due 181 to 360 days | 504,375 | 13 | - | **504,388** |
| - past due over 360 days | 14 | 5 | - | **19** |
| **Total past due but not impaired** | **849,771** | **156** | **-** | **849,927** |
| *Individually impaired loans (total amount)* | | | | |
| - not past due | 24,513,890 | - | 1,198,633 | **25,712,523** |
| - past due 30 days | 217,846 | - | - | **217,846** |
| - past due from 30 to 90 days | 1,433,609 | - | - | **1,433,609** |
| - past due from 91 to 180 days | 4,946,105 | - | - | **4,946,105** |
| - past due 181 to 360 days | 26,293,268 | 1,634,060 | 323,292 | **28,250,620** |
| **Total individually impaired loans (total amount)** | **57,404,718** | **1,634,060** | **1,521,925** | **60,560,703** |
| **Less: provisions for loan impairment** | **(33,154,537)** | **(1,634,060)** | **(1,402,062)** | **(36,190,659)** |
| **Net loans and advances to customers** | **67,187,019** | **42,797** | **554,226** | **67,784,042** |

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### NOTE 12 LOANS AND ADVANCES TO CUSTOMERS (continued)

Since on 31 December 2016 Bank's subsidiary does not have loans issued to nor received collaterals, the realisable value of collateral in respect of loans past due but not impaired and in respect of loans individually determined to be impaired at 31 December 2016 was as follows:

| | Loans to legal entities | Mortgages |
|---|---|---|
| | EUR | EUR |
| *Realisable value of collateral – loans past due but not impaired* | | |
| - Residential real estate | 30,000 | - |
| - Other real estate objects | 6,045,308 | - |
| - Deposits | 3,604,971 | - |
| - Other assets | 3,269,514 | - |
| *Realisable value of collateral – individually impaired loans* | | |
| - Residential real estate | 792,938 | - |
| - Other real estate objects | 40,905,830 | 880,737 |
| - Deposits | 2,800,569 | - |
| - Other assets | 19,041,349 | - |
| **Total** | **76,490,479** | **880,737** |

The realisable value of collateral in respect of loans past due but not impaired and in respect of loans individually determined to be impaired at 31 December 2015 was as follows:

| | Loans to legal entities | Mortgages |
|---|---|---|
| | EUR | EUR |
| *Realisable value of collateral – loans past due but not impaired* | | |
| - Residential real estate | 91,200 | - |
| - Other real estate objects | 1,149,000 | - |
| - deposits | 71,144 | - |
| - Other assets | 3,933,700 | - |
| *Realisable value of collateral – individually impaired loans* | | |
| - Residential real estate | 930,205 | 119,863 |
| - Other real estate objects | 10,544,105 | - |
| - Deposits | 13,001,878 | - |
| - Other assets | 9,763,690 | - |
| **Total** | **39,484,922** | **119,863** |

The Bank's policy is to classify each loan as 'neither past due nor impaired' until specific objective evidence of impairment of the loan is identified.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 12 LOANS AND ADVANCES TO CUSTOMERS** (continued)

The financial effect of collateral is presented by disclosing separately impact (i) on assets with collateral being equal or in excess of the book value of assets ("Assets with collateral value exceeding the loan balance"), and (ii) on assets with collateral being less than the book value of assets ("Assets with insufficient collateral").

The values of collateral disclosed under heading "Realisable value of collateral" represent estimated realisable value which can be obtained from repossession and subsequent sale of the collaterals, and which has been applied in assessment of the impairment of loans. These values are lower than the fair values estimated by independent appraisers. The haircut applied to the fair values to large extent is associated with the uncertainty described in Note 2 Operating Environment of the Bank which, along with other uncertainties, may impact the expenses for foreclosure and sale of collateral as well as the price and timing of the sale of the collateral.

Since on 31 December 2016 Bank's subsidiary does not have loans issued to nor received collaterals, the impact of collateral at 31 December 2016:

| | **Assets with collateral value exceeding the loan balance** | | **Assets with insufficient collateral** | |
|---|---|---|---|---|
| | **Book value of asset (before provisions for impairment)** | **Realisable value of collateral** | **Book value of asset (before provisions for impairment)** | **Realisable value of collateral** |
| | **EUR** | **EUR** | **EUR** | **EUR** |
| Loans to legal entities | 69,552,970 | 141,800,613 | 52,727,162 | 22,473,722 |
| Loans to individuals – consumer loans | 8,451,702 | 15,066,384 | 1,723,315 | - |
| Mortgage loans | 507,708 | 1,410,971 | 1,558,577 | 121,121 |
| **Total** | **78,512,380** | **158,277,968** | **56,009,054** | **22,594,843** |

The impact of collateral at 31 December 2015:

| | **Assets with collateral value exceeding the loan balance** | | **Assets with insufficient collateral** | |
|---|---|---|---|---|
| | **Book value of asset (before provisions for impairment)** | **Realisable value of collateral** | **Book value of asset (before provisions for impairment)** | **Realisable value of collateral** |
| | **EUR** | **EUR** | **EUR** | **EUR** |
| Loans to legal entities | 30,783,507 | 100,497,632 | 69,558,049 | 37,418,782 |
| Loans to individuals – consumer loans | 7,669 | 73,831 | 1,669,188 | 919 |
| Mortgage loans | 434,363 | 905,974 | 1,521,925 | 119,863 |
| **Total** | **31,225,539** | **101,477,437** | **72,749,162** | **37,539,564** |

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### NOTE 13 FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

| | 31.12.2016 Group EUR | 31.12.2016 Bank EUR | 31.12.2015 Group EUR | 31.12.2015 Bank EUR |
|---|---|---|---|---|
| Latvian government debt securities | 13,865,090 | 13,865,090 | 19,381,188 | 19,381,188 |
| OECD state government debt securities | 96,436,701 | 96,436,701 | 241,302,647 | 241,302,647 |
| Non-OECD state government debt securities | 9,868,444 | 9,868,444 | 9,917,633 | 9,917,633 |
| OECD region corporate debt securities | 4,641,261 | 4,641,261 | 9,236,577 | 9,236,577 |
| Non-OECD region corporate debt securities | 423,094 | 423,094 | 9,131,726 | 9,131,726 |
| Unquoted shares | 8,482 | 8,482 | 8,212 | 8,212 |
| | **125,243,072** | **125,243,072** | **288,977,983** | **288,977,983** |

The following table discloses securities by issuers' ratings as at 31 December 2016 and 31 December 2015:

| Rating | 31.12.2016. Securities EUR | 31.12.2016. % | 31.12.2015. Securities EUR | 31.12.2015. % |
|---|---|---|---|---|
| Aaa to Aa3 | 84,880,393 | 67.78 | 228,478,374 | 79.06% |
| From A1 to A3 | 25,153,172 | 20.08 | 38,990,713 | 13.49% |
| From Baa1 to Baa3 | 13,974,134 | 11.16 | 12,368,958 | 4.28% |
| From Ba1 to Ba3 | 278,388 | 0.22 | 9,098,390 | 3.15% |
| Below B3 | - | - | 41,548 | 0.02% |
| | **124,286,086** | 99.24 | **288,977,983** | 100.00% |
| **Without rating** | 956,986 | 0.76 | - | - |
| | **125,243,072** | **100%** | **288,977,983** | **100%** |

### NOTE 14 INTANGIBLE ASSETS

The following changes in the Group's intangible assets took place during 2016 and 2015:

| | Software 2016 EUR | Software 2015 EUR |
|---|---|---|
| **Cost** | | |
| As at the beginning of the year | **1,588,755** | **1,492,506** |
| Additions | 128,246 | 96,249 |
| Advance payment for intangible assets | 229,766 | - |
| **As at end of the year** | **1,946,767** | **1,588,755** |
| **Amortisation** | | |
| Accumulated amortisation at the beginning of the year | **1,333,437** | **1,255,427** |
| Charge for the year | 88,335 | 78,010 |
| **Accumulated amortisation at the end of the year** | **1,421,772** | **1,333,437** |
| **Net book value at the beginning of the year** | **255,318** | **237,079** |
| **Net book value at the end of the year** | **524,995** | **255,318** |

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### NOTE 14 INTANGIBLE ASSETS (continued)

The following changes in the Bank's intangible assets took place during 2016 and 2015:

| | Software | Software |
|---|---|---|
| | 2016 EUR | 2015 EUR |
| **Cost** | | |
| As at the beginning of the year | **1,588,755** | **1,492,506** |
| Additions | 128,246 | 96,249 |
| Advance payment for intangible assets* | 229,766 | - |
| **As at end of the year** | **1,946,767** | **1,588,755** |
| **Amortisation** | | |
| Accumulated amortisation at the beginning of the year | **1,333,437** | **1,255,427** |
| Charge for the year | 88,335 | 78,010 |
| **Accumulated amortisation at the end of the year** | **1,421,772** | **1,333,437** |
| **Net book value at the beginning of the year** | **255,318** | **237,079** |
| **Net book value at the end of the year** | **524,995** | **255,318** |

*At the end of 2016, the Bank made an advance payment for the complex software meant to analyse Bank's customers and their activities. Full system operation launched at the beginning of 2017.

### NOTE 15 PROPERTY AND EQUIPMENT

The following changes in the Group's property and equipment took place during the year ended 31 December 2016:

| | Land and building EUR | Transport EUR | Computers EUR | Office equipment EUR | Other fixed assets EUR | Total EUR |
|---|---|---|---|---|---|---|
| **Cost** | | | | | | |
| 31.12.2015. | **14,748,664** | **89,012** | **780,746** | **588,312** | **100,927** | **16,307,661** |
| Additions | - | - | 79,988 | 7,076 | - | 87,064 |
| Disposals | - | - | (69,216) | (796) | - | (70,012) |
| Advance payments for fixed assets | 313 | - | 164,450 | - | - | 164,763 |
| **31.12.2016.** | **14,748,977** | **89,012** | **955,968** | **594,592** | **100,927** | **16,489,476** |
| **Depreciation** | | | | | | |
| 31.12.2015. | **119,448** | **47,025** | **693,453** | **502,556** | **42,814** | **1,405,296** |
| On disposals | - | - | (69,216) | (796) | **-** | (70,012) |
| Charge for 2016 | 179,172 | 13,036 | 61,577 | 25,893 | 6,116 | 285,794 |
| **31.12.2016.** | **298,620** | **60,061** | **685,814** | **527,653** | **48,930** | **1,621,078** |
| **Net book value 31.12.2015.** | **14,629,216** | **41,987** | **87,293** | **85,756** | **58,113** | **14,902,365** |
| **Net book value 31.12.2016.** | **14,450,357** | **28,951** | **270,154** | **66,939** | **51,997** | **14,868,398** |

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### NOTE 15 PROPERTY AND EQUIPMENT (continued)

The following changes in the Bank's property and equipment took place during the year ended 31 December 2016:

| | Land and building EUR | Transport EUR | Computers EUR | Office equipment EUR | Other fixed assets EUR | Total EUR |
|---|---|---|---|---|---|---|
| **Cost** | | | | | | |
| 31.12.2015. | **14,748,664** | **89,012** | **780,746** | **588,312** | **100,927** | **16,307,661** |
| Additions | - | - | 79,988 | 7,076 | - | 87,064 |
| Disposals | - | - | (69,216) | (796) | - | (70,012) |
| Advance payments for fixed assets | 313 | - | 164,450 | - | - | 164,763 |
| **31.12.2016.** | **14,748,977** | **89,012** | **955,968** | **594,592** | **100,927** | **16,489,476** |
| **Depreciation** | | | | | | |
| 31.12.2015. | **119,448** | **47,025** | **693,453** | **502,556** | **42,814** | **1,405,296** |
| On disposals | - | - | (69,216) | (796) | **-** | (70,012) |
| Charge for 2016 | 179,172 | 13,036 | 61,577 | 25,893 | 6,116 | 285,794 |
| **31.12.2016.** | **298,620** | **60,061** | **685,814** | **527,653** | **48,930** | **1,621,078** |
| **Net book value 31.12.2015.** | **14,629,216** | **41,987** | **87,293** | **85,756** | **58,113** | **14,902,365** |
| **Net book value 31.12.2016.** | **14,450,357** | **28,951** | **270,154** | **66,939** | **51,997** | **14,868,398** |

The following changes in the Group's property and equipment took place during the year ended 31 December 2015:

| | Land and building EUR | Transport EUR | Computers EUR | Office equipment EUR | Other fixed assets EUR | Total EUR |
|---|---|---|---|---|---|---|
| **Cost** | | | | | | |
| 31.12.2014. | **-** | **89,012** | **721,792** | **583,899** | **100,927** | **1,495,630** |
| Additions | 14,748,664 | - | 66,536 | 28,911 | - | 14,844,111 |
| Regrouping | - | - | 1,996 | (1,996) | - | - |
| Disposals | - | - | (9,578) | (22,502) | - | (32,080) |
| **31.12.2015.** | **14,748,664** | **89,012** | **780,746** | **588,312** | **100,927** | **16,307,661** |
| **Depreciation** | | | | | | |
| 31.12.2014. | **-** | **33,989** | **658,750** | **500,024** | **36,699** | **1,229,462** |
| On disposals | | **-** | (9,578) | (22,235) | **-** | (31,815) |
| Regrouping | **-** | **-** | 1,996 | (1,996) | **-** | - |
| Charge for 2015 | 119,448 | 13,036 | 42,286 | 26,763 | 6,115 | 207,648 |
| **31.12.2015.** | **119,448** | **47,025** | **693,453** | **502,556** | **42,814** | **1,405,296** |
| **Net book value 31.12.2014.** | **-** | **55,023** | **63,042** | **83,875** | **64,228** | **266,168** |
| **Net book value 31.12.2015.** | **14,629,216** | **41,987** | **87,293** | **85,756** | **58,113** | **14,902,365** |

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### NOTE 15 PROPERTY AND EQUIPMENT (continued)

The following changes in the Bank's property and equipment took place during the year ended 31 December 2015:

| | Land and building EUR | Transport EUR | Computers EUR | Office equipment EUR | Other fixed assets EUR | Total EUR |
|---|---|---|---|---|---|---|
| **Cost** | | | | | | |
| 31.12.2014. | **-** | **89,012** | **721,792** | **583,899** | **100,927** | **1,495,630** |
| Additions | 14,748,664 | - | 66,536 | 28,911 | - | 14,844,111 |
| Regrouping | - | - | 1,996 | (1,996) | - | - |
| Disposals | - | - | (9,578) | (22,502) | - | (32,080) |
| **31.12.2015.** | **14,748,664** | **89,012** | **780,746** | **588,312** | **100,927** | **16,307,661** |
| **Depreciation** | | | | | | |
| 31.12.2014. | **-** | **33,989** | **658,750** | **500,024** | **36,699** | **1,229,462** |
| On disposals | | **-** | (9,578) | (22,235) | **-** | (31,815) |
| Regrouping | **-** | **-** | 1,996 | (1,996) | **-** | - |
| Charge for 2015 | 119,448 | 13,036 | 42,286 | 26,763 | 6,115 | 207,648 |
| **31.12.2015.** | **119,448** | **47,025** | **693,453** | **502,556** | **42,814** | **1,405,296** |
| **Net book value 31.12.2014.** | **-** | **55,023** | **63,042** | **83,875** | **64,228** | **266,168** |
| **Net book value 31.12.2015.** | **14,629,216** | **41,987** | **87,293** | **85,756** | **58,113** | **14,902,365** |

In March 2015 the Bank signed a contract on purchase of real estate in Riga, J. Alunāna Street 2 for amount of EUR 14,748,664. The real estate is comprised of 2.786 m² land plot and office building.
After the acquisition of the building, category “Leasehold improvements” was renamed into “Other fixed assets”.

### NOTE 16 AVAILABLE-FOR-SALE FINANCIAL ASSETS

The available-for-sale financial assets comprise of VISA Inc preferred shares, which the Bank received in the context of the sale of shares of VISA Europe Limited to VISA Inc.

The Bank has received consideration for the shares of VISA Europe Limited consisting of a cash payment (982,945 EUR), 355 VISA Inc. preference shares and deferred payment of part of the profit (the Bank has recognised a receivable of 84,591 EUR).

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### NOTE 17 OTHER ASSETS

The following table shows the split of the Other assets between the financial assets and non-financial assets on 31 December 2016 and 2015:

| | 31.12.2016 | 31.12.2016 | 31.12.2015 | 31.12.2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| Financial assets, including | 3,215,566 | 3,215,529 | 2,855,860 | 2,855,860 |
| - security deposits | 1,379,357 | 1,379,357 | 721,920 | 721,920 |
| - investment gold | 570,088 | 570,088 | 1,124,320 | 1,124,320 |
| - receivable | 510,133 | 510,133 | 202,629 | 202,629 |
| - other financial assets* | 755,988 | 755,951 | 806,991 | 806,991 |
| Non-financial assets (repossessed collateral) | 2,269,005 | 2,269,005 | 2,537,911 | 2,537,911 |
| **Other assets, gross** | **5,484,571** | **5,484,534** | **5,393,771** | **5,393,771** |
| Impairment of other financial assets | (94,480) | (94,480) | (80,707) | (80,707) |
| **Other assets, net:** | **5,390,091** | **5,390,054** | **5,313,064** | **5,313,064** |

* other financial assets include claims to customers for insurance of collateral and for property tax payments in the total amount of 94,480 EUR (in 2015: 80,707 EUR), for which an impairment provision of 100% has been recognised.

The remaining Other financial assets are not past due or impaired.

Collaterals are recognized initially at fair value, which is regarded as the cost of acquisition. Collaterals are subsequently stated at the lower of cost and net realisable value. The fair value of collaterals is determined based on a valuation performed by an independent appraiser. No write down to net realisable value of collateral has been recognised in the reporting year.

### NOTE 18 CASH AND CASH EQUIVALENTS

| | 31.12.2016 | 31.12.2016 | 31.12.2015 | 31.12.2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| Cash and balances on demand with the Bank of Latvia | 148,906,810 | 148,906,810 | 114,447,515 | 114,447,515 |
| Due from banks with original maturity of 3 months or less | 95,825,755 | 95,825,755 | 129,554,888 | 129,554,888 |
| **Total** | **244,732,565** | **244,732,565** | **244,002,403** | **244,002,403** |

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### NOTE 19 CUSTOMER ACCOUNTS

#### (a) Analysis of groups by customers

| | 31.12.2016 | 31.12.2016 | 31.12.2015 | 31.12.2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| ***Legal entities*** | | | | |
| - current/ settlement accounts | 354,799,013 | 361,379,532 | 481,454,379 | 481,454,379 |
| - term deposits | 25,908,469 | 25,908,469 | 35,934,617 | 35,934,617 |
| ***Private individuals*** | | | | |
| **-** current/ settlement accounts | 35,975,160 | 35,975,160 | 49,863,865 | 49,863,865 |
| **-** term deposits | 5,230,159 | 5,230,159 | 16,726,929 | 16,726,929 |
| **Total customer accounts:** | **421,912,801** | **428,493,320** | **583,979,790** | **583,979,790** |
| ***Sector profile:*** | | | | |
| Private companies | 380,324,762 | 386,905,281 | 517,340,044 | 517,340,044 |
| Private individuals | 41,205,319 | 41,205,319 | 66,590,794 | 66,590,794 |
| Financial institutions | 368,623 | 368,623 | 6 | 6 |
| Non-profit institutions | 4,802 | 4,802 | 32,821 | 32,821 |
| Latvian government | 9,295 | 9,295 | 16,125 | 16,125 |
| **Total customer accounts:** | **421,912,801** | **428,493,320** | **583,979,790** | **583,979,790** |

#### (b) Analysis by place of residence

| | 31.12.2016 | 31.12.2016 | 31.12.2015 | 31.12.2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| Residents | 23,307,659 | 29,888,178 | 26,786,289 | 26,786,289 |
| Non-residents | 398,605,142 | 398,605,142 | 557,193,501 | 557,193,501 |
| **Total customer accounts:** | **421,912,801** | **428,493,320** | **583,979,790** | **583,979,790** |

The average interest rate on term deposits in 2016 was 2.55 % (2015: 2.68 %) and the average interest rate on demand deposits was 0.00 % (2015: 0.04%). All deposits have a fixed interest rate.

Economic sector concentration within customer accounts is as follows:

| | 31.12.2016 | | 31.12.2016 | | 31.12.2015 | | 31.12.2015 | |
|---|---|---|---|---|---|---|---|---|
| | Group | | Bank | | Group | | Bank | |
| | EUR | % | EUR | % | EUR | % | EUR | % |
| Manufacturing | 6,163,729 | 1.46 | 6,163,729 | 1.44 | 6,187,973 | 1.06 | 6,187,973 | 1.06 |
| Building and real estate | 11,646,790 | 2.76 | 18,227,310 | 4.25 | 20,285,064 | 3.47 | 20,285,064 | 3.47 |
| Trade and commercial activities | 223,861,243 | 53.06 | 223,861,243 | 52.24 | 281,292,693 | 48.17 | 281,292,693 | 48.17 |
| Financial and insurance services | 59,151,048 | 14.02 | 59,151,048 | 13.80 | 109,951,416 | 18.,83 | 109,951,416 | 18,83 |
| Transport and communications | 69,164,040 | 16.39 | 69,164,040 | 16.14 | 90,986,483 | 15.58 | 90,986,483 | 15.58 |
| Agriculture and food industries | 986,040 | 0.23 | 986,040 | 0.23 | 791,499 | 0.14 | 791,499 | 0.14 |
| Private individuals | 41,205,319 | 9.77 | 41,205,319 | 9.62 | 66,590,794 | 11.40 | 66,590,794 | 11.40 |
| Other | 9,734,592 | 2.31 | 9,734,592 | 2.28 | 7,893,868 | 1.35 | 7,893,868 | 1.35 |
| **Total customer accounts** | **421,912,801** | **100%** | **428,493,321** | **100%** | **583,979,790** | **100%** | **583,979,790** | **100%** |

Amount attributable to 20 largest depositors as at 31 December 2016 is EUR 176,338,553 (in 2015: EUR 200,499,793), comprising 41.15 % of the total portfolio (in 2015: 34.33%).

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### NOTE 20 DEBT SECURITIES

| | 31.12.2016 | 31.12.2016 | 31.12.2015 | 31.12.2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| Debt securities | 19,072,989 | 19,072,989 | - | - |
| | **19,072,989** | **19,072,989** | **-** | **-** |

During 2016 the Bank issued debt securities in several tranches. The debt securities are offered for sale outside the stock exchange and are not quoted on an open market.

Issued debt securities consist of the following issues:

Subordinated bond series RIB SUBUSD-01/2016 issue amount of 2,200,000 USD. The redemption date of 26 April 2021, the coupon rate of 4.50%, a coupon payment 2 times a year on 26 October and 26 April. Balance at 31 December 2016 of EUR 2,104,046;

Subordinated bonds series RIB SUBUSD-03/2016 issue amount of 14,300,000 USD. The redemption date of 22 June 2021, coupon interest rate of 4.50%, a coupon payment 2 times a year on 22 December and 22 June. Balance at 31 December 2016 of EUR 13,581,337.

Subordinated bonds series RIB SUBUSD-04/2016 issue amount of 3,500,000 USD. The redemption date of 19 July 2021, coupon interest rate of 4.50%, a coupon payment 2 times a year on 19 January and 19 July. Balance at 31 December 2016 of EUR 3,387,606.

### NOTE 21 OTHER FINANCIAL LIABILITIES

| | 31.12.2016 | 31.12.2016 | 31.12.2015 | 31.12.2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| Liabilities in clearance | 53,762 | 53,762 | 454,042 | 454,042 |
| Settlements on behalf of a closed bank | 16,585 | 16,585 | 16,585 | 16,585 |
| Cash in transit | 155,584 | 155,584 | 69,358 | 69,358 |
| Accounts payable | 443,036 | 442,138 | 195,139 | 195,139 |
| | **668,967** | **668,069** | **735,124** | **735,124** |

Liabilities in clearance as at 31 December 2016 and 31 December 2015 include amounts erroneously transferred to the Bank, which were returned to senders at the beginning of 2017 and 2016 respectively.

### NOTE 22 DEFERRED INCOME AND ACCRUED EXPENSES

| | 31.12.2016 | 31.12.2016 | 31.12.2015 | 31.12.2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| Accrued annual leave expenses | 319,181 | 319,181 | 260,544 | 260,544 |
| Accrual for guarantee fund and FCMC financing | 93,025 | 93,025 | 469,478 | 469,478 |
| State social security contributions to be paid | 203,842 | 203,842 | 151,166 | 151,166 |
| Accrued commission expenses | - | - | 132,182 | 132,182 |
| Other accrued expenses | 96,938 | 96,938 | 123,255 | 123,255 |
| | **712,986** | **712,986** | **1,136,625** | **1,136,625** |

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### NOTE 23 DEFERRED INCOME TAX

Deferred income tax for Group and Bank is calculated by using the enacted tax rate – 15%.

The movement on the deferred income tax account is as follows:

| | 31.12.2016 Group EUR | 31.12.2016 Bank EUR | 31.12.2015 Group EUR | 31.12.2015 Bank EUR |
|---|---|---|---|---|
| Deferred income tax liability/ (asset) at the beginning of the reporting year | 33,709 | 33,709 | (19,163) | (19,163) |
| Deferred income tax change during the reporting year (see Note 8) | 197,208 | 197,208 | 52,872 | 52,872 |
| **Deferred tax liability at the end of the reporting year** | **230,917** | **230,917** | **33,709** | **33,709** |

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same taxation authority.

Deferred income tax has been calculated from the following temporary differences between assets and liabilities values for financial reporting and tax purposes:

| | 31.12.2016 Group EUR | 31.12.2016 Bank EUR | 31.12.2015 Group EUR | 31.12.2015 Bank EUR |
|---|---|---|---|---|
| *Deferred income tax liability:* | | | | |
| Temporary difference on fixed assets depreciation | 230,917 | 230,917 | 135,849 | 135,849 |
| *Deferred income tax assets:* | | | | |
| Temporary difference on accruals for unused annual leave | - | - | (48,764) | (48,764) |
| Temporary difference on accrual financial stability fee | - | - | (53,375) | (53,375) |
| **Deferred tax liability/ (asset)** | **230,917** | **230,917** | **33,709** | **33,709** |

### NOTE 24 DERIVATIVE FINANCIAL INSTRUMENTS

The Bank uses the following derivative financial instruments: currency forwards – agreements on currency acquisition in future, currency swaps – agreements on exchange of one set of each cash flow for another. The Bank's credit risk represents the potential cost to replace the forward contracts if counterparties fail to perform their obligation. To control the level of credit risk taken, the Bank assesses counterparties using the same techniques as for its lending activities.

The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognised on the balance sheet but do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments and do not indicate the Bank's exposure to credit risks. The derivative instruments become favourable or unfavourable as a result of fluctuations in market interest rates or foreign exchange rates relative to their terms.

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### NOTE 24 DERIVATIVE FINANCIAL INSTRUMENTS (continued)

The Group’s and the Bank’s notional amounts and fair values of derivative instruments held for trading are set out in the following table:

| | 31.12.2016. | | | 31.12.2015. | | |
|---|---|---|---|---|---|---|
| | Contract/ national amount | Fair value | | Contract/ national amount | Fair value | |
| | | Assets | Liabilities | | | Assets |
| | EUR | EUR | EUR | EUR | EUR | EUR |
| Currency swaps | 103,806,735 | 477,082 | (1,378,768) | 84,202,810 | 237,623 | (1,042,200) |
| Currency forwards | 954,965 | 5,992 | - | 18,645,198 | 25,112 | (67,243) |
| **Total** | **104,761,700** | **483,074** | **(1,378,768)** | **102,848,008** | **262,735** | **(1,109,443)** |

The Bank’s and Group’s notional amounts of derivative instruments by counterparty credit rating are set out in the following table:

| | 31.12.2016. | | | 31.12.2015. | | |
|---|---|---|---|---|---|---|
| **Rating** | Contract/ national amount | Fair value | | Contract/ national amount | Fair value | |
| | | Assets | Liabilities | | | |
| | EUR | EUR | EUR | EUR | EUR | EUR |
| Aaa to Aa3 | 984,848 | 2,138 | - | 3,282,674 | 5,456 | (4,720) |
| A1 to A3 | 60,306,565 | 306,565 | (275,676) | 40,149,444 | 149,444 | (122,440) |
| B1 to B3 | 39,155,545 | 155,545 | (141,779) | 39,088,179 | 88,179 | (64,572) |
| Caa1 and below | - | - | - | 12,049,600 | - | (49,600) |
| Without rating | 4,314,742 | 18,826 | (961,313) | 8,278,111 | 19,656 | (868,111) |
| **Total** | **104,761,700** | **483,074** | **(1,378,768)** | **102,848,008** | **262,735** | **(1,109,443)** |

### NOTE 25 SHARE CAPITAL

Bank’s issued and fully paid share capital as at 31 December 2016 was EUR 32,334,756 EUR (31 December 2015: 32,334,762 EUR). Nominal value of one share is EUR 1.00 (31 December 2015: 1.43 EUR). All shares are ordinary equity shares with voting rights.

On 27 April 2016 a denomination of share capital from lats to euro was registered. As a result of the denomination a difference of 6 EUR has been included in Reserve capital.
In 30 November 2016 shareholder of the Bank Vitalijs Medvedcuks sold all of his shares to Fortum Trade Services LTD. There have been no other changes in the Bank’s shareholders list.

As at 31 December 2016 and 31 December 2015 the shareholders of the Bank were:

| | 31.12.2016 | | 31.12.2015 | |
|---|---|---|---|---|
| | EUR | % | EUR | % |
| "SKY Investment Holding” LLC | 12,094,410 | 37.40 | 12,094,410 | 37.40 |
| Jurij Rodin | 6,466,198 | 20.00 | 6,466,198 | 20.00 |
| AB „Pivdenny” bank | 4,772,908 | 14.76 | 4,772,910 | 14.76 |
| Mark Bekker | 3,095,458 | 9.57 | 3,095,458 | 9.57 |
| ”Jasnii Zori” OOO | 1,937,951 | 5.99 | 1,937,952 | 6.00 |
| DrawNex Universal S.A | 1,565,157 | 4.84 | 1,565,159 | 4.84 |
| Aztin corporation | 711,435 | 2.20 | 711,436 | 2.20 |
| ”Portfolio Investor” OOO | 611,977 | 1.89 | 611,977 | 1.89 |
| PAS „Zakritij nediversificirovannij venčurnij korporativnij investicionnij fond ”Strategičeskije investiciji”” | 509,957 | 1.58 | 509,957 | 1.58 |
| Olegs Atayants | 284,575 | 0.88 | 284,574 | 0.88 |
| Vitalijs Medvedcuks | - | - | 284,574 | 0.88 |
| Fortum Trade Services LTD | 284,575 | 0.89 | - | - |
| Daiga Muravska | 155 | - | 157 | - |
| **Total paid share capital** | **32,334,756** | **100%** | **32,334,762** | **100%** |

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

## NOTE 26 OFF-BALANCE SHEET POSITIONS AND PLEDGED ASSETS

### Guarantees

The following table discloses guarantees issued:

| | 31.12.2016 Group EUR | 31.12.2016 Bank EUR | 31.12.2015 Group EUR | 31.12.2015 Bank EUR |
|---|---|---|---|---|
| Financial guarantees | 5,460,027 | 5,460,027 | 10,725,694 | 10,725,694 |
| | **5,460,027** | **5,460,027** | **10,725,694** | **10,725,694** |

Bank has issued financial guarantees in the amount of EUR 5,460,027. These guarantees are secured by money resources in the security accounts blocked or reserved at the Bank.

In July 2016 Finance and Capital Market Commission (FCMC) initiated an audit to assess the Bank's compliance with the requirements of the "Law on Prevention of Laundering of Proceeds from Criminal Activity (Money Laundering) and of Terrorist Financing" and "Regulations on Enhanced Customer Due Diligence" in respect of the facts published in the media, concerning the suspicious transfer of funds of the "piracy" online portal through the Bank's customer account. In order to assess the activities carried out by the Bank in respect of the customer due diligence process, the FCMC has initiated the administrative process. The Bank has provided to the FCMC the required explanations and documents, and at the date of the signing these financial statements has not received additional requests in respect of the administrative process.

In September 2016, the Financial and Capital Market Commission started a planned inspection of the Bank's compliance with the "Law on Prevention of Laundering of Proceeds from Criminal Activity (Money Laundering) and of Terrorist Financing" and "Regulations on Enhanced Customer Due Diligence . At the date of the signing these financial statements the process continues and the final report on the results of the inspection has not been received.

Despite the fact that the results of the above-mentioned processes have not been received, which creates uncertainty about the future impact of the processes, the Bank's management confirms that the result of this processes will not affect the Bank's ability to meet its obligations towards the Bank's customers and partners. In its operations the Bank adheres to binding laws and regulations, including those relating to prevention of money laundering and terrorist financing. The Bank continuously develops and improves its internal control system, and is making the necessary efforts to avoid any suspicious or unusual customer transactions in the Bank.

### Off-balance sheet credit related commitments

The following table discloses the contractual amounts of the Bank's commitments to extend credit:

| | 31.12.2016 Group EUR | 31.12.2016 Bank EUR | 31.12.2015 Group EUR | 31.12.2015 Bank EUR |
|---|---|---|---|---|
| Loan commitments | 8,675,928 | 8,675,928 | 7,661,902 | 7,661,902 |
| Undrawn credit lines | 12,086,628 | 12,086,628 | 16,874,144 | 16,874,144 |
| **Total credit commitments** | **20,762,556** | **20,762,556** | **24,536,046** | **24,536,046** |

The total outstanding contractual amount of credit commitments and guarantees does not necessarily represent future cash requirements, as these financial instruments may expire or terminate without being funded.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 26 OFF-BALANCE SHEET POSITIONS AND PLEDGED ASSETS** (continued)

The loan commitments are denominated in the following currencies:

| | 31.12.2016 | 31.12.2016 | 31.12.2015 | 31.12.2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| USD | 7,288,434 | 7,288,434 | 6,899,614 | 6,899,614 |
| EUR | 1,387,494 | 1,387,494 | 762,288 | 762,288 |
| **Total** | **8,675,928** | **8,675,928** | **7,661,902** | **7,661,902** |

The undrawn credit lines are denominated in the following currencies

| | 31.12.2016 | 31.12.2016 | 31.12.2015 | 31.12.2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| USD | 5,848,937 | 5,848,937 | 9,204,102 | 9,204,102 |
| EUR | 6,237,691 | 6,237,691 | 7,670,042 | 7,670,042 |
| **Total** | **12,086,628** | **12,086,628** | **16,874,144** | **16,874,144** |

**Assets pledged and restricted**

As at year 2016 and 2015 the Group and the Bank had the following assets pledged:

| | 31.12.2016 | 31.12.2016 | 31.12.2015 | 31.12.2015 |
|---|---|---|---|---|
| | Group | Bank | Group | Bank |
| | EUR | EUR | EUR | EUR |
| Balances due from banks | 15,237,015 | 15,237,015 | 18,257,571 | 18,257,571 |
| Other assets | 1,341,101 | 1,341,101 | 695,613 | 695,613 |
| **Total** | **16,578,116** | **16,578,116** | **18,953,184** | **18,953,184** |

All encumbered assets serve as a pledge for liabilities of the Bank as at 31 December 2016 and 31 December 2015.

Carrying value of encumbered assets approximates their fair value both as at 31 December 2016 and as at 31 December 2015.

Encumbered assets of the Bank as at 31 December 2016 are comprised of the following assets:

- EUR 1,341,101 security deposits for potential claims from Visa Inc and MasterCard Europe SPRL. Agreements with these organisation provide for ensuring sufficient amount of resources available in deposit accounts in the Lloyds TSB Bank plc (Visa Inc) and in U.S Bank (MasterCard Europe Sprl), which could cover all expenses related with the participation of the Bank in these organisations. Total amount of these encumbered assets is included within other assets.
- EUR 4,877,727 security deposits for guarantees issued by the Bank. Total amount of these encumbered assets is included within balances due from other banks.
- EUR 10,359,288 security deposits for execution of securities and derivative financial instruments deals. Total amount of these encumbered assets is included within balances due from other banks.

Encumbered assets of the Bank as at 31 December 2015 are comprised of the following assets:

- EUR 695,613 security deposits for potential claims from Visa Europe Services Inc and MasterCard Europe SPRL. Agreements with these organisation provide for ensuring sufficient amount of resources available in deposit accounts in the Lloyds TSB Bank plc (Visa Europe Services InC) and in HSBC BANK (MasterCard Europe Sprl), which could cover all expenses related with the participation of the Bank in these organisations. Total amount of these encumbered assets is included within other assets.
- EUR 9,785,104 security deposits for guarantees issued by the Bank. Total amount of these encumbered assets is included within balances due from other banks.
- EUR 8,472,467 security deposits for execution of securities and derivative financial instruments deals. Total amount of these encumbered assets is included within balances due from other banks.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

## NOTE 27 CAPITAL ADEQUACY

The Bank's calculation of the capital adequacy ratio according to the Finance and Capital Market Commission Guidelines as at 31 December 2016 and 31 December 2015 have been set in the table below:

| Description | 31.12.2016 | 31.12.2015 |
|---|---|---|
| **Total own funds** | **62,361,492** | **45,673,236** |
| - Tier 1 capital | 35,429,199 | 33,781,198 |
| - Common equity Tier 1 capital | 35,429,199 | 33,781,198 |
| - Tier 2 capital | 26,932,293 | 11,892,038 |
| **Total risk exposure amount** | **204,366,801** | **196,376,490** |
| - Risk weighted exposure amounts for credit, counterparty credit and dilution risks and free deliveries | 160,812,963 | 137,288,426 |
| - Total risk exposure amount for position, foreign exchange and commodities risks | 15,584,413 | 30,777,976 |
| - Total risk exposure amount for operational risk | 27,969,425 | 28,310,088 |
| **Capital adequacy ratios** | | |
| - Common equity Tier 1 Capital ratio | 17.34% | 17.20% |
| - Surplus (+) / Deficit (-) of Common equity Tier 1 capital (4.5%) | 26,232,693 | 24,944,256 |
| - Tier 1 Capital ratio | 17.34% | 17.20% |
| - Surplus (+) / Deficit (-) of Tier 1 capital (6%) | 23,167,191 | 21,998,609 |
| - Total capital ratio | 30.51% | 23.26% |
| - Surplus (+) / Deficit (-) of total capital (8%) | 46,012,148 | 29,963,117 |
| - Total capital ratio | 30.51% | 23.26% |
| - Surplus (+) / Deficit (-) of total capital (11.2%, calculated as a total individual capital requirement set to the Bank of 13.7% less capital retention reserve of 2.5%) | 39,472,410 | 19,947,916 |
| - Capital retention reserve (%) | 2.5% | 2.5% |
| - Capital retention reserve | 5,109,170 | 4,909,412 |

## NOTES TO THE FINANCIAL STATEMENTS (continued)

## NOTE 28 CURRENCY ANALYSIS

The following table provides the analysis of the Group’s assets, liabilities and shareholders’ equity as well as off-balance sheet claims arising from foreign exchange outstanding as at 31 December 2016 by currency profile:

| | USD EUR | EUR EUR | Other EUR | Total EUR |
|---|---|---|---|---|
| **Assets** | | | | |
| Cash and deposits with the Bank of Latvia | 412,217 | 148,494,410 | 183 | 148,906,810 |
| Balances due from banks | 80,715,300 | 4,406,620 | 14,711,727 | 99,833,647 |
| Loans and advances to customers | 58,158,576 | 41,354,872 | - | 99,513,448 |
| Financial assets at fair value through profit or loss | 121,088,754 | 4,154,318 | - | 125,243,072 |
| Available-for-sale financial assets | - | 188,972 | - | 188,972 |
| Intangible assets | - | 524,995 | - | 524,995 |
| Property and equipment | - | 14,868,398 | - | 14,868,398 |
| Derivative financial instruments | - | 483,074 | - | 483,074 |
| Deferred expenses | 32,447 | 214,767 | - | 247,214 |
| Other assets | 1,936,689 | 2,846,685 | 606,717 | 5,390,091 |
| **Total assets** | **262,343,983** | **217,537,111** | **15,318,627** | **495,199,721** |
| **Liabilities and equity** | | | | |
| Balances due to banks | 323,820,380 | 84,947,226 | 13,145,195 | 421,912,801 |
| Debt securities | 19,072,989 | - | - | 19,072,989 |
| Derivative financial instruments | - | 1,378,768 | - | 1,378,768 |
| Deferred income and accrued expenses | 16,602 | 667,938 | 28,446 | 712,986 |
| Corporate income tax liabilities | - | 555,683 | - | 555,683 |
| Deferred tax liability | - | 230,917 | - | 230,917 |
| Other liabilities | 245,466 | 423,501 | - | 668,967 |
| Subordinated loan | 14,072,281 | - | - | 14,072,281 |
| Equity | - | 36,594,329 | - | 36,594,329 |
| **Total liabilities and equity** | **357,227,718** | **124,798,362** | **13,173,641** | **495,199,721** |
| *Net long / (short) position on balance sheet* | **(94,883,735)** | **92,738,749** | **2,144,986** | **-** |
| **Off-balance sheet claims arising from foreign exchange** | | | | |
| Balances due from foreign exchange | 99,784,222 | 3,300,000 | - | 103,084,222 |
| Liabilities from foreign exchange | 4,544,888 | 99,450,000 | - | 103,994,888 |
| *Net long / (short) position on foreign exchange* | *95,239,334* | *(96,150,000)* | *-* | *(910,666)* |
| ***Net long / (short) position*** | **355,599** | **(3,411,251)** | **2,144,986** | **(910,666)** |
| **As at 31 December 2015** | | | | |
| **Total assets** | **436,541,901** | **181,845,606** | **17,187,597** | **635,575,104** |
| **Total liabilities and shareholders’ equity** | **495,047,759** | **124,958,060** | **15,569,285** | **635,575,104** |
| *Net long / (short) position on balance sheet* | **(58,505,858)** | **56,887,546** | **1,618,312** | **-** |
| **Off-balance sheet claims arising from foreign exchange** | | | | |
| Balances due from foreign exchange | 80,806,067 | 20,660,000 | 272,498 | 101,738,565 |
| Liabilities from foreign exchange | 21,835,273 | 80,750,000 | - | 102,585,273 |
| *Net long / (short) position on foreign exchange* | *58,970,794* | *(60,090,000)* | *272,498* | *(846,708)* |
| ***Net long / (short) position*** | **464,936** | **(3,202,454)** | **1,890,810** | **(846,708)** |

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### NOTE 28 CURRENCY ANALYSIS (continued)

The following table provides the analysis of the Bank's assets, liabilities and shareholders' equity as well as off-balance sheet claims arising from foreign exchange outstanding as at 31 December 2016 by currency profile:

| | USD EUR | EUR EUR | Other EUR | Total EUR |
|---|---|---|---|---|
| **Assets** | | | | |
| Cash and deposits with the Bank of Latvia | 412,217 | 148,494,410 | 183 | 148,906,810 |
| Balances due from banks | 80,715,300 | 4,406,620 | 14,711,727 | 99,833,647 |
| Loans and advances to customers | 58,158,576 | 41,354,872 | - | 99,513,448 |
| Financial assets at fair value through profit or loss | 121,088,754 | 4,154,318 | - | 125,243,072 |
| Investment in subsidiary | - | 6,600,000 | - | 6,600,000 |
| Available-for-sale financial assets | - | 188,972 | - | 188,972 |
| Intangible assets | - | 524,995 | - | 524,995 |
| Property and equipment | - | 14,868,398 | - | 14,868,398 |
| Derivative financial instruments | - | 483,074 | - | 483,074 |
| Deferred expenses | 32,447 | 214,767 | - | 247,214 |
| Other assets | 1,936,689 | 2,846,648 | 606,717 | 5,390,054 |
| **Total assets** | **262,343,983** | **224,137,074** | **15,318,627** | **501,799,684** |
| **Liabilities and equity** | | | | |
| Customer accounts | 323,820,380 | 91,527,745 | 13,145,195 | 428,493,320 |
| Debt securities | 19,072,989 | - | - | 19,072,989 |
| Derivative financial instruments | - | 1,378,768 | - | 1,378,768 |
| Deferred income and accrued expenses | 16,602 | 667,938 | 28,446 | 712,986 |
| Corporate income tax liabilities | - | 555,683 | - | 555,683 |
| Deferred tax liability | - | 230,917 | - | 230,917 |
| Other liabilities | 245,466 | 422,603 | - | 668,069 |
| Subordinated loan | 14,072,281 | - | - | 14,072,281 |
| Equity | - | 36,614,671 | - | 36,614,671 |
| **Total liabilities and equity** | **357,227,718** | **131,398,325** | **13,173,641** | **501,799,684** |
| *Net long / (short) position on balance sheet* | **(94,883,735)** | **92,738,749** | **2,144,986** | **-** |
| **Off-balance sheet claims arising from foreign exchange** | | | | |
| Balances due from foreign exchange | 99,784,222 | 3,300,000 | - | 103,084,222 |
| Liabilities from foreign exchange | 4,544,888 | 99,450,000 | - | 103,994,888 |
| *Net long / (short) position on foreign exchange* | *95,239,334* | *(96,150,000)* | *-* | *(910,666)* |
| ***Net long / (short) position*** | **355,599** | **(3,411,251)** | **2,144,986** | **(910,666)** |
| **As at 31 December 2015** | | | | |
| **Total assets** | **436,541,901** | **181,845,606** | **17,187,597** | **635,575,104** |
| **Total liabilities and shareholders' equity** | **495,047,759** | **124,958,060** | **15,569,285** | **635,575,104** |
| *Net long / (short) position on balance sheet* | **(58,505,858)** | **56,887,546** | **1,618,312** | **-** |
| **Off-balance sheet claims arising from foreign exchange** | | | | |
| Balances due from foreign exchange | 80,806,067 | 20,660,000 | 272,498 | 101,738,565 |
| Liabilities from foreign exchange | 21,835,273 | 80,750,000 | - | 102,585,273 |
| *Net long / (short) position on foreign exchange* | *58,970,794* | *(60,090,000)* | *272,498* | *(846,708)* |
| ***Net long / (short) position*** | **464,936** | **(3,202,454)** | **1,890,810** | **(846,708)** |

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

## NOTE 29 LIQUIDITY RISK AND ANALYSIS OF ASSETS AND LIABILITIES BY MATURITY PROFILE

The table below allocates the Group's assets and liabilities to maturity groupings as at 31 December 2016 based on the time remaining from the balance sheet date to the contractual maturity dates:

| | Overdue | 1 m. | 1 – 3 m. | 3 – 6 m. | 6 –12 m. | 1–5 years | More than 5 years | Total |
|---|---|---|---|---|---|---|---|---|
| | EUR | EUR | EUR | EUR | EUR | EUR | EUR | EUR |
| **Assets** | | | | | | | | |
| Cash and balances with the Bank of Latvia | - | 148,906,810 | - | - | - | - | - | **148,906,810** |
| Balances due from banks | - | 88,138,183 | 7,616,155 | - | 4,079,309 | - | - | **99,833,647** |
| Loans and advances to customers | 7,962,315 | 1,552,447 | 3,173,814 | 4,162,799 | 36,935,557 | 44,739,240 | 987,276 | **99,513,448** |
| Financial assets at fair value through profit or loss | - | 55,143,693 | 25,851,571 | 7,518,337 | 11,065,764 | 25,161,951 | 501,756 | **125,243,072** |
| Available-for-sale financial assets | - | - | - | - | - | - | 188,972 | **188,972** |
| Intangible assets | - | - | - | - | - | - | 524,995 | **524,995** |
| Property and equipment | - | - | - | - | - | - | 14,868,398 | **14,868,398** |
| Derivative financial instruments | - | 483,074 | - | - | - | - | - | **483,074** |
| Deferred expenses | - | - | - | - | 247,214 | - | - | **247,214** |
| Other assets | 223,340 | 1,470,854 | - | 83,007 | 42,154 | 2,229,635 | 1,341,101 | **5,390,091** |
| **Total assets** | **8,185,655** | **295,695,061** | **36,641,540** | **11,764,143** | **52,369,998** | **72,130,826** | **18,412,498** | **495,199,721** |
| **Liabilities and equity** | | | | | | | | |
| Customer accounts | - | 395,267,621 | 9,699,156 | 601,524 | 9,389,564 | 6,954,936 | - | **421,912,801** |
| Debt securities | - | 67,238 | - | 32,219 | - | 18,973,532 | - | **19,072,989** |
| Derivative financial instruments | - | 1,378,768 | - | - | - | - | - | **1,378,768** |
| Deferred income and accrued expenses | - | 190,031 | - | - | 522,955 | - | - | **712,986** |
| Current income tax liability | - | - | 555,683 | - | - | - | - | **555,683** |
| Deferred tax liability | - | - | - | - | 230,917 | - | - | **230,917** |
| Other financial liabilities | - | 668,967 | - | - | - | - | - | **668,967** |
| Subordinated loan | - | 7,202 | - | - | - | 14,065,079 | - | **14,072,281** |
| Share capital and reserves | - | - | - | - | - | - | 36,594,329 | **36,594,329** |
| **Total liabilities and equity** | **-** | **397,579,827** | **10,254,839** | **633,743** | **10,143,436** | **39,993,547** | **36,594,329** | **495,199,721** |
| *Off-balance sheet liabilities* | **-** | **829,354** | **4,268,258** | **8,421,483** | **6,341,407** | **6,280,591** | **81,490** | **26,222,583** |
| **Net liquidity** | **8,185,655** | **(102,714,120)** | **22,118,443** | **2,708,917** | **35,885,155** | **25,856,688** | **(18,263,321)** | **(26,222,583)** |
| **As at 31 December 2015** | | | | | | | | |
| **Total assets** | **9,750,074** | **435,004,892** | **24,993,361** | **16,372,876** | **53,239,769** | **76,960,811** | **19,253,321** | **635,575,104** |
| **Total liabilities and equity** | **-** | **542,521,223** | **5,436,371** | **3,880,383** | **20,623,074** | **22,115,953** | **40,998,100** | **635,575,104** |
| *Off-balance sheet liabilities* | **-** | **2,122,398** | **3,620,948** | **8,516,857** | **10,769,332** | **10,050,724** | **181,481** | **35,261,740** |
| **Net liquidity** | **9,750,074** | **(109,638,729)** | **15,936,042** | **3,975,636** | **21,847,363** | **44,794,134** | **(21,926,260)** | **(35,261,740)** |

## NOTES TO THE FINANCIAL STATEMENTS (continued)

## NOTE 29 LIQUIDITY RISK AND ANALYSIS OF ASSETS AND LIABILITIES BY MATURITY PROFILE (continued)

The table below allocates the Bank's assets and liabilities to maturity groupings as at 31 December 2016 based on the time remaining from the balance sheet date to the contractual maturity dates:

| | Overdue | 1 m. | 1 – 3 m. | 3 – 6 m. | 6 –12 m. | 1–5 years | More than 5 years | Total |
|---|---|---|---|---|---|---|---|---|
| | EUR | EUR | EUR | EUR | EUR | EUR | EUR | EUR |
| **Assets** | | | | | | | | |
| Cash and balances with the Bank of Latvia | - | 148,906,810 | - | - | - | - | - | **148,906,810** |
| Balances due from banks | - | 88,138,183 | 7,616,155 | - | 4,079,309 | - | - | **99,833,647** |
| Loans and advances to customers | 7,962,315 | 1,552,447 | 3,173,814 | 4,162,799 | 36,935,557 | 44,739,240 | 987,276 | **99,513,448** |
| Financial assets at fair value through profit or loss | - | 55,143,693 | 25,851,571 | 7,518,337 | 11,065,764 | 25,161,951 | 501,756 | **125,243,072** |
| Investment in subsidiary | - | - | - | - | - | - | 6,600,000 | **6,600,000** |
| Available-for-sale financial assets | - | - | - | - | - | - | 188,972 | **188,972** |
| Intangible assets | - | - | - | - | - | - | 524,995 | **524,995** |
| Property and equipment | - | - | - | - | - | - | 14,868,398 | **14,868,398** |
| Derivative financial instruments | - | 483,074 | - | - | - | - | - | **483,074** |
| Deferred expenses | - | - | - | - | 247,214 | - | - | **247,214** |
| Other assets | 223,303 | 1,470,854 | - | 83,007 | 42,154 | 2,229,635 | 1,341,101 | **5,390,054** |
| **Total assets** | **8,185,618** | **295,695,061** | **36,641,540** | **11,764,143** | **52,369,998** | **72,130,826** | **25,012,498** | **501,799,684** |
| **Liabilities and equity** | | | | | | | | |
| **Total assets** | | | | | | | | |
| Debt securities | - | 67,238 | - | 32,219 | - | 18,973,532 | - | **19,072,989** |
| Customer accounts | - | 401,848,140 | 9,699,156 | 601,524 | 9,389,564 | 6,954,936 | - | **428,493,320** |
| Derivative financial instruments | - | 1,378,768 | - | - | - | - | - | **1,378,768** |
| Deferred income and accrued expenses | - | 190,031 | - | - | 522,955 | - | - | **712,986** |
| Corporate income tax liabilities | - | - | 555,683 | - | - | - | - | **555,683** |
| Deferred tax liability | - | - | - | - | 230,917 | - | - | **230,917** |
| Other liabilities | - | 668,069 | - | - | - | - | - | **668,069** |
| Subordinated loan | - | 7,202 | - | - | - | 14,065,079 | - | **14,072,281** |
| Equity | - | - | - | - | - | - | 36,614,671 | **36,614,671** |
| **Total liabilities and equity** | **-** | **404,159,448** | **10,254,839** | **633,743** | **10,143,436** | **39,993,547** | **36,614,671** | **501,799,684** |
| *Off-balance sheet liabilities* | **-** | **829,354** | **4,268,258** | **8,421,483** | **6,341,407** | **6,280,591** | **81,490** | **26,222,583** |
| **Net liquidity** | **8,185,618** | **(109,293,741)** | **22,118,443** | **2,708,917** | **35,885,155** | **25,856,688** | **(11,683,663)** | **(26,222,583)** |

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 29 LIQUIDITY RISK AND ANALYSIS OF ASSETS AND LIABILITIES BY MATURITY PROFILE** (continued)

| | Overdue EUR | 1 m. EUR | 1 – 3 m. EUR | 3 – 6 m. EUR | 6 –12 m. EUR | 1–5 years EUR | More than 5 years EUR | Total EUR |
|---|---|---|---|---|---|---|---|---|
| **As at 31 December 2015** | | | | | | | | |
| **Total assets** | **9,750,074** | **435,004,892** | **24,993,361** | **16,372,876** | **53,239,769** | **76,960,811** | **19,253,321** | **635,575,104** |
| **Total liabilities and equity** | **-** | **542,521,223** | **5,436,371** | **3,880,383** | **20,623,074** | **22,115,953** | **40,998,100** | **635,575,104** |
| *Off-balance sheet liabilities* | **-** | **2,122,398** | **3,620,948** | **8,516,857** | **10,769,332** | **10,050,724** | **181,481** | **35,261,740** |
| **Net liquidity** | **9,750,074** | **(109,638,729)** | **15,936,042** | **3,975,636** | **21,847,363** | **44,794,134** | **(21,926,260)** | **(35,261,740)** |

Management of the Bank is confident that short-term liquidity is not endangered. Liquidity calculated based on the requirements of the FCMC as at 31 December 2016 was 81.33% (as at 31 December 2015: 90.42%). In accordance with the requirements of the FCMC, the Bank has to ensure sufficient amount of liquid assets to fulfil liabilities, but not less than in amount of 60% from the amount of the total current liabilities of the Bank.

Deposits serving as pledge for liabilities of customers are disclosed based on maturity of the underlying liability. The table below allocates the Bank’s financial liabilities on undiscounted cash flow bases as at 31 December 2016:

| | Overdue EUR | 1 m. EUR | 1 – 3 m. EUR | 3 – 6 m. EUR | 6 –12 m. EUR | 1–5 years EUR | More than 5 years EUR | Total EUR |
|---|---|---|---|---|---|---|---|---|
| Debt securities | - | 74,708 | - | 352,196 | 426,904 | 22,036,571 | - | 22,890,379 |
| Customer accounts | - | 401,891,789 | 9,866,056 | 689,298 | 9,676,697 | 7,575,053 | - | 429,698,893 |
| Other liabilities | - | 668,069 | - | - | - | - | - | 668,069 |
| Subordinated loan | - | 92,225 | 165,491 | 251,469 | 506,537 | 16,582,252 | - | 17,597,974 |
| **Total liabilities** | **-** | **402,726,791** | **10,031,547** | **1,292,963** | **10,610,138** | **46,193,876** | **-** | **470,855,315** |
| *Off-balance sheet liabilities* | **-** | **829,354** | **4,268,258** | **8,421,483** | **6,341,407** | **6,280,591** | **81,490** | **26,222,583** |

The table below allocates the Bank’s financial liabilities on undiscounted cash flow bases as at 31 December 2015:

| | Overdue EUR | 1 m. EUR | 1 – 3 m. EUR | 3 – 6 m. EUR | 6 –12 m. EUR | 1–5 years EUR | More than 5 years EUR | Total EUR |
|---|---|---|---|---|---|---|---|---|
| Customer accounts | - | 540,115,170 | 5,573,859 | 3,988,318 | 21,132,187 | 14,866,818 | 71,246 | 585,747,598 |
| Other liabilities | - | 735,122 | - | - | - | - | - | 735,122 |
| Subordinated loan | - | 40,895 | 69,655 | 104,699 | 209,832 | 8,739,692 | 5,970,423 | 15,135,197 |
| **Total liabilities** | **-** | **540,891,187** | **5,643,514** | **4,093,017** | **21,342,019** | **23,606,510** | **6,041,669** | **601,617,916** |
| *Off-balance sheet liabilities* | **-** | **2,122,398** | **3,620,948** | **8,516,857** | **10,769,332** | **10,050,724** | **181,481** | **35,261,740** |

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### NOTE 29 LIQUIDITY RISK AND ANALYSIS OF ASSETS AND LIABILITIES BY MATURITY PROFILE (continued)

The table below allocates the Group's and Bank's derivative instruments undiscounted future cash flows as at 31 December 2016:

| | Up to 1 month | 1 to 3 months | Over 3 months | Total |
|---|---|---|---|---|
| | EUR | EUR | EUR | EUR |
| **Derivatives settled on a gross basis** | | | | |
| Foreign exchange derivatives: | | | | |
| - inflow | 103,382,931 | - | - | **103,382,931** |
| - outflow | 104,278,626 | - | - | **104,278,626** |

The table below allocates the Group's and Bank's derivative instruments future cash flows as at 31 December 2015:

| | Up to 1 month | 1 to 3 months | Over 3 months | Total |
|---|---|---|---|---|
| | EUR | EUR | EUR | EUR |
| **Derivatives settled on a gross basis** | | | | |
| Foreign exchange derivatives: | | | | |
| - inflow | 99,128,565 | 2,310,000 | 300,000 | **101,738,565** |
| - outflow | 99,948,936 | 2,326,444 | 309,893 | **102,585,273** |

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

## NOTE 30 RE-PRICING MATURITY OF ASSETS AND LIABILITIES

The table below allocates the Group's assets and liabilities to maturity groupings as at 31 December 2016 based on the time remaining from the balance sheet date to the earlier of maturity and contractual re-pricing dates:

| | 1 m. | 1–3 m. | 3–6 m. | 6–12 m. | 1–5 years | Over 5 years | Positions which are not sensitive to the interest risk | Total |
|---|---|---|---|---|---|---|---|---|
| | EUR | EUR | EUR | EUR | EUR | EUR | EUR | EUR |
| **Assets** | | | | | | | | |
| Cash and balances with the Bank of Latvia | 147,836,974 | - | - | - | - | - | 1,069,836 | **148,906,810** |
| Balances due from banks | 83,365,819 | - | - | - | - | - | 16,467,828 | **99,833,647** |
| Loans and advances to customers | 14,078,184 | 17,778,593 | 6,880,098 | 26,720,414 | 33,312,038 | 626,573 | 117,548 | **99,513,448** |
| Financial assets at fair value through profit or loss | 55,143,695 | 25,851,572 | 7,518,338 | 11,065,763 | 25,161,947 | 493,275 | 8,482 | **125,243,072** |
| Available-for-sale financial assets | - | - | - | - | - | - | 188,972 | **188,972** |
| Intangible assets | - | - | - | - | - | - | 524,995 | **524,995** |
| Property and equipment | - | - | - | - | - | - | 14,868,398 | **14,868,398** |
| Other assets | - | - | - | - | - | - | 6,120,379 | **6,120,379** |
| **Total assets** | **300,424,672** | **43,630,165** | **14,398,436** | **37,786,177** | **58,473,985** | **1,119,848** | **39,366,438** | **495,199,721** |
| **Liabilities and equity** | | | | | | | | |
| Customer accounts | 1,642,853 | 522,711 | 598,498 | 3,664,282 | 5,226,484 | - | 410,257,973 | **421,912,801** |
| Debt securities | - | - | - | - | 18,973,532 | - | 99,457 | **19,072,989** |
| Deferred tax liabilities | - | - | - | - | - | - | 230,917 | **230,917** |
| Other liabilities | - | - | - | - | - | - | 3,316,404 | **3,316,404** |
| Subordinated loan | - | - | - | - | 14,065,079 | - | 7,202 | **14,072,281** |
| **Total liabilities** | **1,642,853** | **522,711** | **598,498** | **3,664,282** | **38,265,095** | **-** | **413,911,953** | **458,605,392** |
| **Equity** | **-** | **-** | **-** | **-** | **-** | **-** | 36,594,329 | **36,594,329** |
| **Total liabilities and equity** | **1,642,853** | **522,711** | **598,498** | **3,664,282** | **38,265,095** | **-** | **450,506,282** | **495,199,721** |
| ***On balance sheet interest sensitivity analysis*** | **298,781,819** | **43,107,454** | **13,799,938** | **34,121,895** | **20,208,890** | **1,119,848** | **(411,139,844)** | - |
| **As at 31 December 2015** | | | | | | | | |
| **Total assets** | **445,939,630** | **37,208,431** | **15,940,626** | **34,460,368** | **63,928,674** | **1,447,189** | **36,650,186** | **635,575,104** |
| **Total liabilities and equity** | **8,591,609** | **5,365,847** | **1,806,006** | **9,133,498** | **21,906,824** | **6,041,568** | **582,729,752** | **635,575,104** |
| ***On balance sheet interest sensitivity analysis*** | **437,348,021** | **31,842,584** | **14,134,620** | **25,326,870** | **42,021,850** | **(4,594,379)** | **(546,079,566)** | - |

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### NOTE 30 RE-PRICING MATURITY OF ASSETS AND LIABILITIES (continued)

The table below allocates the Bank's assets and liabilities to maturity groupings as at 31 December 2016 based on the time remaining from the balance sheet date to the earlier of maturity and contractual re-pricing dates:

| | 1 m. EUR | 1–3 m. EUR | 3–6 m. EUR | 6–12 m. EUR | 1–5 years EUR | Over 5 years EUR | Positions which are not sensitive to the interest risk EUR | Total EUR |
|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | |
| Cash and balances with the Bank of Latvia | 147,836,974 | - | - | - | - | - | 1,069,836 | **148,906,810** |
| Balances due from banks | 83,365,819 | - | - | - | - | - | 16,467,828 | **99,833,647** |
| Loans and advances to customers | 14,078,184 | 17,778,593 | 6,880,098 | 26,720,414 | 33,312,038 | 626,573 | 117,548 | **99,513,448** |
| Financial assets at fair value through profit or loss | 55,143,695 | 25,851,572 | 7,518,338 | 11,065,763 | 25,161,947 | 493,275 | 8,482 | **125,243,072** |
| Available-for-sale financial assets | - | - | - | - | - | - | 188,972 | **188,972** |
| Investment in subsidiary | - | - | - | - | - | - | 6,600,000 | **6,600,000** |
| Intangible assets | - | - | - | - | - | - | 524,995 | **524,995** |
| Property and equipment | - | - | - | - | - | - | 14,868,398 | **14,868,398** |
| Other assets | - | - | - | - | - | - | 6,120,342 | **6,120,342** |
| **Total assets** | **300,424,672** | **43,630,165** | **14,398,436** | **37,786,177** | **58,473,985** | **1,119,848** | **45,966,401** | **501,799,684** |
| **Liabilities and equity** | | | | | | | | |
| Customer accounts* | 1,642,853 | 522,711 | 598,498 | 3,664,282 | 5,226,484 | - | 416,838,492 | **428,493,320** |
| Debt securities | - | - | - | - | 18,973,532 | - | 99,457 | **19,072,989** |
| Deferred tax liabilities | - | - | - | - | - | - | 230,917 | **230,917** |
| Other liabilities | - | - | - | - | - | - | 3,315,506 | **3,315.506** |
| Subordinated loan | - | - | - | - | 14,065,079 | - | 7,202 | **14,072,281** |
| **Total liabilities** | **1,642,853** | **522,711** | **598,498** | **3,664,282** | **38,265,095** | | **420,491,574** | **465,185,013** |
| **Equity** | **-** | **-** | **-** | **-** | **-** | **-** | 36,614,671 | **36,614,671** |
| **Total liabilities and equity** | **1,642,853** | **522,711** | **598,498** | **3,664,282** | **38,265,095** | **-** | **457,106,245** | **501,799,684** |
| ***On balance sheet interest sensitivity analysis*** | ***298,781,819*** | ***43,107,454*** | ***13,799,938*** | ***34,121,895*** | ***20,208,890*** | ***1,119,848*** | ***(411,139,844)*** | - |
| **As at 31 December 2015** | | | | | | | | |
| **Total assets** | **445,939,630** | **37,208,431** | **15,940,626** | **34,460,368** | **63,928,674** | **1,447,189** | **36,650,186** | **635,575,104** |
| **Total liabilities and equity** | **8,591,609** | **5,365,847** | **1,806,006** | **9,133,498** | **21,906,824** | **6,041,568** | **582,729,752** | **635,575,104** |
| ***On balance sheet interest sensitivity analysis*** | ***437,348,021*** | ***31,842,584*** | ***14,134,620*** | ***25,326,870*** | ***42,021,850*** | ***(4,594,379)*** | ***(546,079,566)*** | - |

* The Customer accounts positions which are not sensitive to the interest risk include guarantee deposits in amount of EUR 18,175,017.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

## NOTE 31 RELATED PARTY TRANSACTIONS

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions.

Related parties are defined as shareholders, members of the Council and the Board, key management personnel, their close relatives and companies in which they have a controlling interest as well as companies, where they have significant influence.

Parent company of the Bank is AB Pivdenny bank, because it controls the operations of the Bank. Ultimate beneficiary of the Bank is Jurij Rodin.

Operations with the related parties were as follows as at 31 December 2016:

| | Parent company of the Bank | Entities under control of the Bank's shareholders | Subsidiary of the Bank | Other related parties |
|---|---|---|---|---|
| Total loans and advances (interest rate on agreement: 5,7-24%) | 11,715,365 | 2,916,232 | - | 6,984 |
| Correspondent account | 6,916,489 | - | - | - |
| Investment in the share capital of the subsidiary | - | - | 6,600,000 | - |
| Customer accounts (interest rate: 0.0%) | - | 2,789,047 | 6,580,519 | 91,619 |
| Subordinated loan (interest rate on agreement: 7.0-8.5%) | 1,423,647 | 6,027,178 | - | - |

Income and expense from operations with related parties during 2016 were as follows:

| | Parent company of the Bank | Entities under control of the Bank's shareholders | Subsidiary of the Bank | Other related parties |
|---|---|---|---|---|
| Interest income | 1,544,528 | 178,809 | - | 553 |
| Interest expenses | 552,445 | 182,197 | - | - |
| Provisions for loan impairment | - | 954,558 | - | - |
| Fee and commission income | - | 38,182 | 57 | 405 |
| Fee and commission expense | 36,001 | - | - | - |
| Administrative and other operating expenses | 18,938 | - | - | - |

The balances in respect of off-balance sheet liabilities towards related parties are as follows as at 31 December 2016:

| | Entities under control of the Bank's shareholders | Other related parties |
|---|---|---|
| Undrawn credit lines | - | 6,150 |
| Assets under management | 5,937,928 | - |

Total amounts of loans issued to and repaid by related parties during 2016 are as follows:

| | Parent company of the Bank | Entities under control of the Bank's shareholders | Other related parties |
|---|---|---|---|
| Issued to related parties | 11,713,678 | - | 72,181 |
| Repaid by related parties | 13,067,802 | 320,216 | 68,306 |

Transactions with the parent company of the Bank include total amount of short term loans issued and repaid during 2016.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**NOTE 31 RELATED PARTY TRANSACTIONS** (continued)

Operations with the related parties were as follows as at 31 December 2015:

| | Parent company of the Bank | Entities under control of the Bank's shareholders | Other related parties |
|---|---|---|---|
| Total loans and advances (interest rate on agreement: 5,7-24%) | 13,006,346 | 3,166,334 | 3,110 |
| Correspondent account | 10,243,085 | - | - |
| Customer accounts (interest rate: 0.0%) | - | 4,697,172 | 63,006 |
| Subordinated loan (interest rate on agreement: 8.0-8.5%) | 8,108,748 | 1,061,851 | - |

Income and expense from operations with related parties during 2015 were as follows:

| | Parent company of the Bank | Entities under control of the Bank's shareholders | Other related parties |
|---|---|---|---|
| Interest income | 1,859,205 | 227,443 | 439 |
| Interest expenses | 706,134 | 217,494 | - |
| Fee and commission income | - | 17,971 | 181 |
| Fee and commission expense | 13,038 | - | - |
| Administrative and other operating expenses | 16,941 | - | - |

The balances in respect of off-balance sheet liabilities towards related parties are as follows as at 31 December 2015:

| | Entities under control of the Bank's shareholders | Other related parties |
|---|---|---|
| Undrawn credit lines | - | 6,597 |
| Assets under management | 5,878,558 | - |

Total amounts of loans issued to and repaid by related parties during 2015 are as follows:

| | Parent company of the Bank | Entities under control of the Bank's shareholders | Other related parties |
|---|---|---|---|
| Issued to related parties | 453,619,923 | - | 43,677 |
| Repaid by related parties | 465,122,244 | 21,736 | 45,600 |

Transactions with the parent company of the Bank include total amount of short term loans issued and repaid during 2015.

## NOTES TO THE FINANCIAL STATEMENTS (continued)

### NOTE 31 RELATED PARTY TRANSACTIONS (continued)

Remuneration to the Board and Council is disclosed below:

| | 31.12.2016 Group | 31.12.2016 Bank | 31.12.2015 Group | 31.12.2015 Bank |
|---|---|---|---|---|
| *Short-term benefits:* | **EUR** | **EUR** | **EUR** | **EUR** |
| - Salaries | 587,076 | 587,076 | 432,040 | 432,040 |
| *Pension benefits:* | | | | |
| - Expenses to the State Pension Insurance | 140,819 | 140,819 | 69,695 | 69,695 |
| **Total** | **727,895** | **727,895** | **501,735** | **501,735** |

### NOTE 32 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The best evidence of fair value is price in an active market. An active market is one in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. The Bank discloses information on fair values of assets and liabilities in such a way as to enable its comparison with book values.

When determining fair values of assets and liabilities, the Bank is using various sources of fair value, which are grouped into three categories based of following hierarchy:
Level 1 – quoted market prices in an active market;
Level 2 – models to determine fair value using data directly observable in the market;
Level 3 – other methods for determining fair value using data, which is not directly observable in the market.

Instruments within **Level 1** include highly liquid assets and financial instruments traded on the stock exchange.

Fair value for such financial instruments as Financial assets at fair value through profit and loss is mainly determined based on publicly available quoted prices (bid price obtained from Bloomberg system).

Instruments within **Level 2** include assets, for which no active market exists, such as over the counter derivative financial instruments and currency swaps agreements, as well as balances on demand with the Bank of Latvia, amounts due from credit institutions, Financial assets at fair value through profit and loss, amounts due to credit institutions and deposits and current accounts, as well as other financial assets and liabilities.

Fair value of derivative financial instruments is determined based on discounted cash flow models with all parameters used (foreign currency exchange rate, interest rate) being directly observable in the market.

Fair value of cash and demand deposits with the Bank of Latvia is determined based on expected present value of discounted future cash flows. Discount rate applied in the calculation is based on the interest rates prevailing in the market at the end of the year.

Fair value of amounts due to credit institutions is determined based on expected present value of discounted future cash flows. Discount rate applied in the calculation is based on the interest rates prevailing in the market at the end of the year.

Fair value of deposits is determined based on expected present value of discounted future cash flows. Discount rate applied in the calculation is based on the interest rates prevailing in the market at the end of the year.

Fair value of other financial assets and liabilities is determined based on expected present value of discounted future cash flows. Discount rate applied in the calculation is based on the interest rates prevailing in the market at the end of the year.

## NOTES TO THE FINANCIAL STATEMENTS (continued)

## NOTE 32 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES (continued)

**Level 3** instruments are available-for-sale financial assets, as well as loans and subordinated debt.

Fair value of available-for-sale financial instruments was determined based on indicative price offer received from the potential buyer and which is considered to be the best representation of the fair value.

Fair value of loans is determined based on expected present value of discounted future cash flows. Discount rate applied in the calculation is based on the interest rates prevailing in the market at the end of the year adjusted to take into account credit risk.

Fair value of subordinated loan is determined based on expected present value of discounted future cash flows. Discount rate applied in the calculation is based on the interest rate of last similar deal adjusted by the decline of the market rates observed during the period since that deal.

Fair value of issued debt securities is determined based on expected present value of discounted future cash flows. Discount rate applied in the calculation is based on the interest rate of the most recently issued debt securities.

The table below shows Group's assets and liabilities valued at amortised cost by book values and fair values as at 31 December 2016 and 31 December 2015:

| | Book value EUR | 31.12.2016. Fair value EUR | Book value EUR | 31.12.2015. Fair value EUR |
|---|---|---|---|---|
| **Assets valued at amortised cost** | | | | |
| Cash and balances with the Bank of Latvia | 148,906,810 | 148,906,810 | 114,447,515 | 114,447,515 |
| Balances due from Banks | 99,833,647 | 99,833,647 | 142,561,234 | 142,561,234 |
| Loans to legal entities | 90,341,121 | 92,315,872 | 67,187,019 | 72,716,981 |
| Loans to private individuals, except for mortgages | 8,543,499 | 8,667,848 | 42,797 | 47,068 |
| Mortgages | 628,828 | 636,242 | 554,226 | 683,019 |
| Other financial assets | 3,121,086 | 3,121,086 | 2,775,153 | 2,775,153 |
| **Total assets valued at amortised cost** | **351,374,991** | **353,481,505** | **327,567,944** | **333,230,970** |
| **Liabilities valued at amortised cost** | | | | |
| Customer accounts | 421,912,801 | 423,756,096 | 583,979,790 | 585,474,321 |
| Debt securities | 19,072,989 | 19,072,989 | - | - |
| Subordinated loan | 14,072,281 | 14,179,853 | 13,623,927 | 13,621,367 |
| Other financial liabilities | 668,069 | 668,069 | 735,124 | 735,124 |
| **Total liabilities valued at amortised cost** | **455,726,140** | **457,677,007** | **598,338,841** | **599,830,812** |

## NOTES TO THE FINANCIAL STATEMENTS (continued)

## NOTE 32 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES (continued)

The table below shows Bank's assets and liabilities valued at amortised cost by book values and fair values as at 31 December 2016 and 31 December 2015:

| | 31.12.2016. | | 31.12.2015. | |
|---|---|---|---|---|
| | **Book value EUR** | **Fair value EUR** | **Book value EUR** | **Fair value EUR** |
| **Assets valued at amortised cost** | | | | |
| Cash and balances with the Bank of Latvia | 148,906,810 | 148,906,810 | 114,447,515 | 114,447,515 |
| Balances due from Banks | 99,833,647 | 99,833,647 | 142,561,234 | 142,561,234 |
| Loans to legal entities | 90,341,121 | 92,315,872 | 67,187,019 | 72,716,981 |
| Loans to private individuals, except for mortgages | 8,543,499 | 8,667,848 | 42,797 | 47,068 |
| Mortgages | 628,828 | 636,242 | 554,226 | 683,019 |
| Other financial assets | 3,121,049 | 3,121,049 | 2,775,153 | 2,775,153 |
| **Total assets valued at amortised cost** | **351,374,954** | **353,481,468** | **327,567,944** | **333,230,970** |
| **Liabilities valued at amortised cost** | | | | |
| Customer accounts | 428,493,320 | 430,336,615 | 583,979,790 | 585,474,321 |
| Debt securities | 19,072,989 | 19,072,989 | - | - |
| Subordinated loan | 14,072,281 | 14,179,853 | 13,623,927 | 13,621,367 |
| Other financial liabilities | 668,069 | 668,069 | 735,124 | 735,124 |
| **Total liabilities valued at amortised cost** | **462,306,659** | **464,257,526** | **598,338,841** | **599,830,812** |

## NOTES TO THE FINANCIAL STATEMENTS (continued)

## NOTE 32 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES (continued)

The table below specified Group's analysis by fair value levels as at 31 December 2016 and 31 December 2015 (based on carrying amounts):

| | 31.12.2016. | | | 31.12.2015. | | |
|---|---|---|---|---|---|---|
| | **Level 1 EUR** | **Level 2 EUR** | **Level 3 EUR** | **Level 1 EUR** | **Level 2 EUR** | **Level 3 EUR** |
| **Assets valued at fair value** | | | | | | |
| Derivative financial instruments | - | 483,074 | - | - | 262,735 | - |
| Available-for-sale financial assets | - | - | 188,972 | - | - | 919,980 |
| Financial assets at fair value through profit or loss | 110,881,832 | 14,361,240 | - | 288,977,983 | - | - |
| **Total assets valued at fair value** | **110,881,832** | **14,844,314** | **188,972** | **288,977,983** | **262,735** | **919,980** |
| **Assets valued at amortised cost** | | | | | | |
| Cash and balances with the Bank of Latvia | - | 148,906,810 | - | - | 114,447,515 | - |
| Balances due from banks | - | 99,833,647 | - | - | 142,561,234 | - |
| Loans and advances to customers | - | - | 99,513,448 | - | - | 67,784,042 |
| Other financial assets | - | 3,121,086 | - | - | 2,775,153 | - |
| **Total assets valued at amortised cost** | **-** | **251,861,543** | **99,513,448** | **-** | **259,783,902** | **67,784,042** |
| **Liabilities valued at fair value** | | | | | | |
| Derivative financial instruments | - | 1,378,768 | - | - | 1,109,443 | - |
| **Total liabilities valued at fair value** | **-** | **1,378,768** | **-** | **-** | **1,109,443** | **-** |
| **Liabilities valued at amortised cost** | | | | | | |
| Customer accounts | - | 421,912,801 | - | - | 583,979,790 | - |
| Debt securities | - | - | 19,072,989 | | | |
| Subordinated loan | - | - | 14,072,281 | - | - | 13,623,927 |
| Other financial liabilities | - | 668,069 | - | - | 735,124 | - |
| **Total liabilities valued at amortised cost** | **-** | **422,580,870** | **33,145,270** | - | **584,714,914** | **13,623,927** |

## NOTES TO THE FINANCIAL STATEMENTS (continued)

## NOTE 32 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES (continued)

The table below specified Bank’s analysis by fair value levels as at 31 December 2016 and 31 December 2015 (based on carrying amounts):

| | 31.12.2016. | | | 31.12.2015. | | |
|---|---|---|---|---|---|---|
| | **Level 1 EUR** | **Level 2 EUR** | **Level 3 EUR** | **Level 1 EUR** | **Level 2 EUR** | **Level 3 EUR** |
| **Assets valued at fair value** | | | | | | |
| Derivative financial instruments | - | 483,074 | - | - | 262,735 | - |
| Available-for-sale financial assets | - | - | 188,972 | - | - | 919,980 |
| Financial assets at fair value through profit or loss | 110,881,832 | 14,361,240 | - | 288,977,983 | - | - |
| **Total assets valued at fair value** | **110,881,832** | **14,844,314** | **188,972** | **288,977,983** | **262,735** | **919,980** |
| **Assets valued at amortised cost** | | | | | | |
| Cash and balances with the Bank of Latvia | - | 148,906,810 | - | - | 114,447,515 | - |
| Balances due from banks | - | 99,833,647 | - | - | 142,561,234 | - |
| Loans and advances to customers | - | - | 99,513,448 | - | - | 67,784,042 |
| Other financial assets | - | 3,121,049 | - | - | 2,775,153 | - |
| **Total assets valued at amortised cost** | **-** | **251,861,506** | **99,513,448** | **-** | **259,783,902** | **67,784,042** |
| **Liabilities valued at fair value** | | | | | | |
| Derivative financial instruments | - | 1,378,768 | - | - | 1,109,443 | - |
| **Total liabilities valued at fair value** | **-** | **1,378,768** | **-** | **-** | **1,109,443** | **-** |
| **Liabilities valued at amortised cost** | | | | | | |
| Customer accounts | - | 428,493,320 | - | - | 583,979,790 | - |
| Debt securities | - | - | 19,072,989 | | | |
| Subordinated loan | - | - | 14,072,281 | - | - | 13,623,927 |
| Other financial liabilities | - | 668,069 | - | - | 735,124 | - |
| **Total liabilities valued at amortised cost** | **-** | **429,161,389** | **33,145,270** | - | **584,714,914** | **13,623,927** |

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

## NOTE 33 TAXES

The following table reflects the tax calculated and paid by the Group for 2016:

| | Balance as at 31.12.2015. EUR | Calculated in 2016 EUR | Returned from the budget EUR | Paid in 2016 EUR | Balance as at 31.12.2016. EUR |
|---|---|---|---|---|---|
| Corporate income tax* | - | 809,234 | - | 253,551 | 555,683 |
| State compulsory social insurance contributions | 86,617 | 1,457,935 | - | 1,415,500 | 129,052 |
| Personal income tax | - | 818,305 | - | 818,155 | 150 |
| Value added tax | (3,822) | 167,049 | 6,028 | 81,336 | 87,919 |
| **(Overpaid)** | **(3,822)** | | | | **-** |
| **Liabilities** | **86,617** | | | | **772,804** |

The following table reflects the tax calculated and paid by the Bank for 2016:

| | Balance as at 31.12.2015. EUR | Calculated in 2016 EUR | Returned from the budget EUR | Paid in 2016 EUR | Balance as at 31.12.2016. EUR |
|---|---|---|---|---|---|
| Corporate income tax* | - | 809,234 | - | 253,551 | 555,683 |
| State compulsory social insurance contributions | 86,617 | 1,456,870 | - | 1,414,683 | 128,804 |
| Personal income tax | - | 817,661 | - | 817,661 | - |
| Value added tax | (3,822) | 167,086 | 6,028 | 81,336 | 87,956 |
| **(Overpaid)** | **(3,822)** | | | | **-** |
| **Liabilities** | **86,617** | | | | **772,443** |

* CIT calculated and paid includes the amount of tax withheld abroad – 247,748 EUR.

The tax authorities have the right to inspect the tax computations for the last three taxation years. The Bank's management is not aware of any circumstances which may give rise to a potential material liability in this respect.

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

## NOTE 34 SUBORDINATED LOANS

The subordinated loans as at 31 December of 2016 and 2015 included:

| | 31.12.2016 Group | | 31.12.2016 Bank | | 31.12.2015 Group | | 31.12.2015 Bank | |
|---|---|---|---|---|---|---|---|---|
| | EUR | % | EUR | % | EUR | % | EUR | % |
| Fortum Trade Services LTD (maturity year 2019-2021) | 6,027,178 | 7.00-8.50 | 6,027,178 | 7.00-8.50 | 1,061,851 | 7.00 | 1,061,851 | 7.00 |
| AB „Pivdenny" banka (maturity year 2021) | 1,423,648 | 8.00 | 1,423,648 | 8.00 | 8,108,748 | 8.00-8.50 | 8,108,748 | 8.00-8.50 |
| Venture Resource Investments LTD (maturity year 2019) | 1,900,726 | 8.00 | 1,900,726 | 8.00 | 1,840,319 | 8.00 | 1,840,319 | 8.00 |
| Aleksejs Fedoricevs (maturity year 2019) | - | - | - | - | 1,837,411 | 7.00 | 1,837,411 | 7.00 |
| UK Industries Group LTD (maturity year 2021) | 1,898,618 | 8.00 | 1,898,618 | 8.00 | - | - | - | - |
| Crownfield Nordic Limited Partnership (maturity year 2018) | 1,897,722 | 7.00 | 1,897,722 | 7.00 | - | - | - | - |
| Maxiplan L.P (maturity year 2020) | 402,518 | 8.50 | 402,518 | 8.50 | 389,726 | 8.50 | 389,726 | 8.50 |
| Igors Chudenkovs (maturity year 2020) | 398,538 | 8.50 | 398,538 | 8.50 | 385,872 | 8.50 | 385,872 | 8.50 |
| Andrejs Volodins (maturity year 2020) | 123,333 | 8.50 | 123,333 | 8.50 | - | - | - | - |
| **Total** | **14,072,281** | | **14,072,281** | | **13,623,927** | | **13,623,927** | |

## NOTE 35 ASSETS UNDER MANAGEMENT

Assets held by the Bank under management are financial instruments held on behalf of customers and other customer assets acquired under trust agreements.

| | 31.12.2016 Group | 31.12.2016 Bank | 31.12.2015 Group | 31.12.2015 Bank |
|---|---|---|---|---|
| ***Legal entities:*** | **EUR** | **EUR** | **EUR** | **EUR** |
| - non-residents | 103,524,097 | 103,524,097 | 100,582,655 | 100,582,655 |
| ***Private individuals:*** | | | | |
| - residents | 199,966 | 199,966 | - | - |
| - non-residents | 7,846,034 | 7,846,034 | 7,304,456 | 7,304,456 |
| **Total** | **111,570,097** | **111,570,097** | **107,887,111** | **107,887,111** |

## NOTE 36 RETURN ON CAPITAL AND RETURN ON ASSETS

| | 31.12.2016 Group | 31.12.2016 Bank | 31.12.2015 Group | 31.12.2015 Bank |
|---|---|---|---|---|
| Return on capital (ROE) (%) | 7.06 % | 7.12 % | (4.39) % | (4.39) % |
| Return on assets (ROA) (%) | 0.50 % | 0.50 % | (0.24) % | (0.24) % |

Both return ratios are calculated based on FCMC regulations, taking annual average from monthly balances. ROE is calculated as net profit for the year divided by annual average total equity. ROA is calculated as net profit for the year divided by annual average total assets.

## NOTE 37 SUBSEQUENT EVENTS

During the period since the last day of the year there have not been events that significantly affect the Group's and Bank's financial position as at 31 December 2016.