Translation from Latvian original

JSC “REGIONALA INVESTICIJU BANKA”

ANNUAL REPORT FOR THE YEAR ENDED 31 DECEMBER 2015

Contents

JSC “Regionala investiciju banka”

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JSC “Regionala investiciju banka”

REPORT OF THE MANAGEMENT

In 2015, JSC "Regionala investiciju banka" (hereinafter – the Bank) continued successful development, which is confirmed by a moderate growth of the main financial indicators. The value of the Bank's assets in the reporting year increased by 7.3% and as of 31 December of the year 2015 amounted to EUR 635 million. The operating profit (profit before tax and provisions for doubtful loans) in 2015 as compared to the previous year increased by 7.6% and reached EUR 6.7 million. Over the reporting period, the Bank created provisions for doubtful loans in the amount of EUR 8 million.

Due to the plans of VISA Inc. to buy out the Bank's share of VISA Europe Limited, in these financial statements the Bank has recognized income from the price increase of the share by 920,000. As a result, the Bank closed the year with the comprehensive loss of EUR 650,000.

General Economic Situation

In 2015, significant events for Latvia took place in overseas markets. Throughout the year, the economy of Latvia was negatively affected by geopolitical tensions between Russia and Ukraine, reciprocal sanctions of Russia and the EU, and the fall of the Russian rouble along with the economic downturn in Russia. Despite continued economic growth in the EU and the Eurozone, the Greece's insolvency crisis in the first half of the year had a negative effect on the Eurozone, while the problem of uncontrolled immigration in summer has led to the temporary restrictions of the Schengen area functioning. At the same time, the entire world economy suffered from the downturn in the economic growth of China and sharp fluctuations in the stock markets. Slow growth of the global economy, high level of resources and the rising volume of production have caused a dramatic drop in oil prices, i.e. more than 60%. The decrease of oil prices led to a fall in the prices of other energy sources and products on the global stock markets. The currency markets also endured intense volatility in 2015, where the EUR to USD exchange rate plummeted to its lowest during the past twelve years.

It was a complicated year for the economy of Latvia, but on the average successful. It is developing as predicted, and its growth can be characterized as moderate. Regardless of unfavourable external conditions, the growth during the first three quarters of 2015 increased by 2.7%. In 2015, Latvian exporters managed to circumvent the sanctions imposed by Russia and not to be affected by an overall drop in demand in this neighbouring country, whose economy is going through a recession. Although exports to Russia during the first nine months decreased by 24.4%, Latvia is the only Baltic country that was able to increase the total volume of exports by 2%. The project regarding the implementation of the EU funds is successfully continuing. It is expected that GDP growth in Latvia will remain moderate in the future, at around 3%. The Bank of Latvia predicts inflation of 1.3%. It has been noted that the economic growth continues to be exposed to relatively high risks. In addition to external risks, local factors can also have an adverse impact on the national economy. Such factors include the decline of the working-age population and the low level of investment, as well as too fast and inappropriate increase in labour costs, which is not commensurate with labour productivity.

The assets in the Latvian banking sector at the end of December of 2015 reached EUR 31.9 billion, which is 3.6% more than at the end of 2014. The total volume of loans over the year increased by 0.7% and amounted to EUR 14.7 billion (at the end of 2014 – EUR 14.6 billion). The quality of loans is getting better; the share of overdue loans (over 90 days) decreased by 12.5% and at the end of 2015 it was EUR 883.5 million (6% of the total loan portfolio). The liquid securities portfolios on balance sheets of banks continued to grow. The securities portfolio of the central government over the year has grown by 49.5%, reaching EUR 3.4 billion. The liquidity ratio of the banking system at the end of 2015 was at 66.7%. Capital indicators of Latvia's banking sector significantly exceeded the minimum capital requirements. The total sector capital rate (KPR) at the end of the third quarter reached 21.6%, while the Core Tier (CET1) was 18.8%.

The profitability indicators have improved: the banking sector at large in 2015 received profit of EUR 415.9 million, and ROE at the end of 2015 was 12.5% (at the end of 2014 – 11.1%).

Bank's Activity during the Reporting Year

In comparison with 2014, the deposit portfolio of the Bank in 2015 grew by 8% and as of 31 December 2015 it was EUR 584 million. Meanwhile, the volume of assets increased by 7.3% and at the end of the reporting period amounted to EUR 635 million.

During 2015, the Bank continued to expand its customer base, and over the year the number of Customers increased by 15.7%. The largest growth was seen in the segment of foreign Customers, namely in the legal entities sector.

Report of the management (continued)

Bank's Activity during the Reporting Year (continued)

As of 31 December 2015, the loan portfolio of the Bank (consisting of granted loans and loan issue commitments) was EUR 92 million. During the reporting period, Customers paid off their liabilities in the total amount of EUR 7.3 million. The Bank issued new loans in the total amount of EUR 8.6 million and signed agreements about granting EUR 7.7 million in loans.

In 2015, the securities portfolio of the Bank increased rapidly, i.e. by 44.5% and as of 31 December 2015 it reached EUR 289 million. This substantial growth in 2015 took place due to investments into short-term and medium-term government bonds with high credit ratings.

At the beginning of 2015, the Bank started offering its Customers an opportunity to purchase precious metals as financial instruments and yet another currency in the current account, as well as bullions of precious metals. To ensure that a larger segment of our Customers can afford buying precious metals, we offer gold bullions of various denominations: 20, 50, 100, 250, 500 and 1000 grams. Apart from gold, the Bank also provides an opportunity to buy silver, platinum and palladium.

The first quarter of 2015 was marked with a memorable event. In March, the Bank bought a building at J. Alunana Street 2, where it used to rent premises for conducting its business. The building is located in the quiet Center of Riga, in the upscale district favoured by embassies, and it has the status of a cultural and historical monument. In the future, the Bank plans to use the premises for its own needs and rent the extra space to reliable business partners.

In April of 2015, the Bank organized a depository, and began offering Customers an option to store valuables and documents in individual fireproof safes that are under 24-hour guarding and surveillance and are equipped with the latest modern alarm system. The depository of individual safes is located in the Bank's building at 2 J. Alunana Street in Riga. The Bank offers flexible rent periods of individual bank safes, from one month up to one year, with an option to extend the rent period.

On June 5, 2015, the number of Members of the Board was increased by one more, the fourth, member – Gints Gritans, the Head of Treasury Department. When the Council approved the new member, changes were made to the organizational structure of the Bank with the purpose to improve the governance functions: each Member of the Board, in accordance with his competence, was offered to supervise certain subdivisions of the Bank. Over the reporting period, with the idea to optimize the internal processes, the Bank has introduced the following changes in the organizational structure: Compliance Control Division was created on the basis of three departments, i.e. Compliance Control Department, Monitoring Department and Money Laundering Prevention Department; Finance Planning and Control Department was given a status of a separate subdivision of the Bank; two separate sections were created in Payment Cards Department: Payment Card Issuance Section and Payment Cards Acceptance Section; three sections were created in Loans Department: Lending Section for Non-Residents, Lending Section for Residents and Monitoring and Reporting Section; two new sections were added to the IT Department: Infrastructure and Telecommunications Section, and IS User Support Section; and the Investment Management Section was created. In 2015, forty-eight new employees joined the Bank, eight people were hired by Procurement Department and Security Department after the Bank purchased the building at 2 J. Alunana Street. As of 31 December 172 people were employed by the Bank.

In 2015, the Bank managed to attract new Customers due to the provision of documentary operations; and this fact had a positive effect on risk diversification of the Customer Portfolio. Therefore, despite political and economic situation in the world, the Bank has gained more than EUR 453,000 on documentary operations. In comparison with 2014, the portfolio of issued warranties increased by 124% and as of 31 December 2015 reached EUR 10.7 million.

During the reporting period, he Bank witnessed considerable growth in the number of active payment cards – by 60%; the payment card turnover increased by 28% and as of 31 December 2015 reached EUR 33.3 million. The Bank was actively working on improvement of the payment card acceptance service, and the annual turnover as compared to the same period of the previous year increased by 21.6%.

Report of the management (continued)

Bank's Activity during the Reporting Year (continued)

A number of substantial improvements were achieved during the reporting period in the IT area. These improvements have made easier and have optimized execution of internal and external IT processes. The Bank has upgraded and renewed security systems, it was constantly working on improvement and development of the internal IT infrastructure, and the computer fleet was updated. The Internet Bank offered the option of the two-tier signature of documents and we have launched a project aimed at increasing the speed of the Internet banking facility.

In November 2015, the FCMC defined for the bank an individual requirement for the capital at 15.6%, which also includes the capital reserve at the rate of 2.5%. The Bank met this requirement of the FCMC in 2015. The FCMC requirement to the individual liquidity ratio was established at 60%. As of 31 December 2015, the liquidity ratio of the Bank was 90.35%.

Coverage of losses proposed by the Board

The Board proposes to cover loss for the reporting year with retained earnings.

Plans and Prospects for 2016

To improve the quality of customer service, increase the number of Customers and to be able to offer banking services that meet individual needs of our Customers, the Bank will keep working on improvement of the service offered by private bankers. In the first half of 2015, the Bank received permission of the FCMC allowing it to render consulting services to Customers in regard to investing into financial instruments and the permission to manage the portfolio of Customers' investments. These developments are in line with the goals of the Bank to perfect the segment of investment products.

At the end of 2015, the Bank presented for approval of the FCMC the bond program prospectus, and it was registered by the FCMC Council at the very beginning of 2016. The prospectus provides that the Bank is entitled to hold public offering of bonds for 20 million US dollars. It means that the Bank can launch its first issuance of bonds. Specific parameters of the first bond issuance will be formulated in the respective bond issuance documents and will become available when the Bank starts the first drawdown.

The goal of the Bank for 2016 is to increase the number of Customers and to develop investment products. The Bank intends to work actively on launching programs of structured deposits and develop the sphere of investment consulting service.

Olexandr Kovalsky
Chairman of the Board

Iurii Rodin
Chairman of the Council

Riga, 23 March 2016

THE SUPERVISORY COUNCIL AND THE BOARD OF DIRECTORS OF THE BANK

As at 31 December 2015 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

During 2015 there have been the following changes in the members of the Board of Directors of AS Reģionālā investīciju banka:

On 5 June 2015 Gints Gritans was elected as the Member of the Board.

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 financial statements of the Bank.

The financial statements on pages 10 to 62 are prepared in accordance with the source documents and present fairly the financial position of the Bank as at 31 December 2015 and the results of its operations and cash flows for the reporting year 2015.

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
Chairman of the Board

Iurii Rodin
Chairman of the Council

Riga, 23 March 2016

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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

We have audited the accompanying financial statements on pages 10 to 62 of AS Regionala Investiciju banka (the Bank), which comprise the statement of financial position as at 31 December 2015 and the statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation of financial statements that give a true and fair view in accordance with 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 financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of financial statements that give a true and fair view 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

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Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the AS Regionala Investiciju banka as at 31 December 2015, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

Emphasis of Matter – Operating Environment

We draw your attention to the Note 2 to the financial statements. The operations of the Bank, and those of other entities in Ukraine, have been affected and may continue to be affected for the foreseeable future, by the continuing uncertainties in Ukraine. Our opinion is not qualified in respect of this matter.

Report on Other Legal and Regulatory Requirements

We have read the Report of the Management set out on pages 3 to 5 and did not identify material inconsistencies between the financial information contained in the Report of the Management and that contained in the accompanying financial statements.

PricewaterhouseCoopers SIA
Certified audit company
Licence No. 5

Juris Lapše
Certified auditor in charge
Certificate No. 116
Persona per procura

Riga, Latvia
23 March 2016

* 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.

Statement of Comprehensive Income for the year ended 31 December 2015

	Notes	2015 EUR	2014 EUR
Interest income	5	8,293,530	11,254,166
Interest expense	5	(5,389,982)	(4,875,161)
Net interest income		**2,903,548**	**6,379,005**
Provisions for loan impairment	11	(7,914,812)	(7,521,689)
Net interest income after provision for loan impairment		**(5,011,264)**	**(1,142,684)**
Fee and commission income	6	9,690,351	7,267,083
Fee and commission expense	6	(1,483,825)	(1,418,179)
Net fee and commission income	6	**8,206,526**	**5,848,904**
Gain on sale of trading securities, net		-	133,319
Loss from revaluation of trading securities, net		(274,675)	(443,761)
(Loss)/ gain from derivative financial instruments revaluation, net		(1,067,896)	127,511
Gain from trading in foreign currencies, net		2,978,952	2,519,502
Gain/ (loss) from foreign exchange translation, net		701,440	(592,512)
Impairment loss on other assets		(179,232)	-
Other operating income		275,830	138,056
Loss from sale of repossessed collateral	35	17,184	(1,438,130)
Administrative expenses	7	(6,446,576)	(6,166,695)
Amortization and depreciation charges	13, 14	(285,658)	(197,330)
Other operating expense		(146,545)	(98,930)
Loss before income tax		**(1,231,914)**	**(1,312,750)**
Corporate income tax	8	(337,893)	(569,490)
Net loss for the year		**(1,569,807)**	**(1,882,240)**
Items that can be reclassified subsequently to profit or loss:			
Net gain from investment securities available-for-sale	34	919,970	-
Total comprehensive loss for the year attributable to the owners of the Bank		**(649,837)**	**(1,882,240)**

The financial statements on pages 10 to 62 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, 23 March 2016

The accompanying notes on pages 14 to 62 are an integral part of these financial statements.

Statement of Financial Position as at 31 December 2015

	Notes	31.12.2015 EUR	31.12.2014 EUR
Assets			
Cash and balances with the Bank of Latvia	9	114,447,515	101,306,508
Balances due from banks	10	142,561,234	216,007,335
Loans and advances to customers	11	67,784,042	70,395,363
Financial assets at fair value through profit or loss	12	288,977,983	199,941,747
Available for sale financial assets	34	919,980	-
Derivative financial instruments	20	262,735	736,612
Intangible assets	13	255,318	237,079
Property and equipment	14	14,902,365	266,168
Other assets	32	5,313,064	3,434,550
Deferred expenses		150,868	154,824
Deferred income tax asset	19	-	19,163
Total assets		**635,575,104**	**592,499,349**
Liabilities			
Balances due to banks	16	-	7,365
Customer accounts	15	583,979,790	540,933,163
Derivative financial instruments	20	1,109,443	515,424
Other financial liabilities	17	735,124	2,345,540
Deferred income and accrued expenses	18	1,136,625	874,774
Subordinated loan	31	13,623,927	12,216,760
Deferred tax liability	19	33,709	-
Total liabilities		**600,618,618**	**556,893,026**
Equity			
Share capital	21	32,334,762	32,334,762
Revaluation reserve on available-for-sale financial assets		919,970	-
Retained earnings		1,701,754	3,271,561
Total equity		**34,956,486**	**35,606,323**
Total liabilities and equity		**635,575,104**	**592,499,349**
Off balance sheet items			
Guarantees issued	22	10,725,694	4,694,429
Credit related commitments	22	24,536,046	26,892,521
Assets under management	33	107,887,111	129,283,269

The financial statements on pages 10 to 62 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, 23 March 2016

The accompanying notes on pages 14 to 62 are an integral part of these financial statements.

Statement of Changes in Equity for the year ended 31 December 2015

	Paid-in share capital	Retained earnings	Revaluation reserve on available-for-sale financial assets	Total
	EUR	EUR	EUR	EUR
Balance as at 31 December 2013	**32,334,762**	**5,153,801**	**-**	**37,488,563**
Comprehensive loss for the year	-	(1,882,240)	-	(1,882,240)
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 accompanying notes on pages 14 to 62 are an integral part of these financial statements..

Statement of Cash Flows for the year ended 31 December 2015

	Notes	2015 EUR	2014 EUR
Cash flows from operating activities			
Interest received		5,198,813	8,415,570
Interest paid		(5,550,783)	(5,043,382)
Fees and commission received		9,690,351	7,267,083
Fees and commission paid		(1,483,825)	(1,418,179)
Income on trading securities		-	133,319
Income on foreign exchange		2,978,952	2,519,502
Other operating income		275,830	1,386,344
Personnel expenses paid		(4,573,179)	(4,010,604)
Administrative and other operating expenses		(2,342,427)	(4,929,433)
Income tax paid		(285,021)	(569,342)
Cash flows generated from operating activities before changes in operating assets and liabilities		**3,908,711**	**3,750,878**
Changes in operating assets and liabilities			
Net increase of securities at fair value through profit or loss		(64,807,665)	(194,286,458)
Net decrease of balances due from banks		17,667,836	41,040,813
Net decrease/ (increase) of loans and advances to customers		9,040,081	(14,886,407)
Net (increase)/ decrease of other assets		(4,169,877)	978,754
Net (decrease)/ increase of customer accounts		(8,088,150)	194,183,341
Net (decrease)/ increase in other liabilities		(1,363,003)	4,652,016
Net cash and cash equivalents (used in)/ generated from operating activities		**(47,812,067)**	**35,432,937**
Cash flows from investing activities			
Purchase of intangible assets		(88,202)	(115,011)
Purchase of fixed assets		(14,843,116)	(91,894)
Net cash and cash equivalents used in investing activities		**(14,931,318)**	**(206,905)**
Effect of exchange rates on cash and cash equivalents		15,519,582	(18,091,335)
Net (decrease)/ increase in cash and cash equivalents		**(47,223,803)**	**17,134,697**
Cash and cash equivalents at the beginning of the year	**23**	291,226,206	274,091,509
Cash and cash equivalents at the end of the year	**23**	**244,002,403**	**291,226,206**

The accompanying notes on pages 14 to 62 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 new representative office in Kiev, Ukraine. Furthermore, in 2010 the Bank has established its representative office in the capital of Belgium – Brussels. The Bank has no subsidiaries and branches apart from the mentioned above.

The Bank is a joint-stock company incorporated and domiciled in Riga, Republic of Latvia. It was registered within Commercial Register on 28 September 2001.

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

These financial statements have been approved for issue by the Council and the Board of Directors on ___ March 2016.

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 in Ukraine as at 31 December 2015 and as at 31 December 2014:

	31.12.2015 thousand EUR	31.12.2014. thousand EUR
Balance sheet assets subject to the Ukraine country risk:		
Balances due from banks	876	8,009
Loans issued	19,960	22,772
Financial assets at fair value through profit or loss	-	30
Total	**20,836**	**30,811**
Off-balance sheet items subject to the Ukraine country risk:		
Off-balance sheet commitments to clients	3,956	7,265
Total	**3,956**	**7,265**

Situation in Ukraine remains complex .At the end of the 2015 inflation in Ukraine reached 43.3% - the highest in the past 20 years (in December 2014 the inflation rate was 24.9%, but in December 2013 - 0.5%). Meanwhile, the World Bank estimates show that during 2015 gross domestic product shrunk by 12%. Despite this, the World Bank predicts - if Ukraine will implement the proposed reforms and will fight corruption, the economy during 2016 could return to a 1% growth.

2016 promises to be a challenging year for Ukraine's economy – as a response to Ukraine's accession to the European Union's free trade zone, from 1 January the Russian Government implement embargo on export of certain food products from Ukraine, as well as stopped the operations of a free-trade agreement signed in 2011 with Ukraine. The Government of Ukraine, in return, responded to the sanctions by establishing import ban for various Russian goods. During 2016 Kiev is supposed to receive major loan – the International Monetary Fund will contribute 4.5 billion U.S. dollars, 1.5 billion will be guaranteed by the European Union, but one billion dollars will be provided by US. While in relation to the three billion U.S. dollar debt to Russia Ukraine announced moratorium. Russia reacted by threatening with court proceedings.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 2 OPERATING ENVIRONMENT OF THE BANK (continued)

Credit rating agencies Fitch and Standard & Poor's in autumn 2015 temporarily lowered the rating of Ukraine to "partial default" after the State failed to make a payment within ten days long debt holiday period on the 500 million U.S. dollars' worth of bonds. Then, after the State completed the restructuring of its bonds and resumed debt servicing, "partial default" rating was lifted (now Moody's - Caa3, Fitch – CCC and Standard &Poor's - B-).

The banking system in Ukraine is still fragile, it was affected by the devaluation of the national currency, the strong recession, as well as by the military conflict in the eastern part of Ukraine. Total losses of Ukraine's banking sector in 2015 reached 66.6 billion hryvnia, thus exceeding the current maximum amount of losses that in 2014 amounted to 52.96 billion hryvnia. Amount of bad loans varies approximately at 44%, while the amount of provisions for these loans is about 68%. The banks have undertaken restructuring of external debt. Since 2014 Ukraine's central bank liquidated around 60 banks. Expenses for recapitalization of banks and deposit insurance affect public finances. The process of liquidation of banks is expected to continue also in 2016. For those banks, who continue their operations, the central bank introduced new risk-assessment procedures, forcing shareholders to increase the capital of banks. Despite the difficulties which had come across all Ukraine's banking sector participants, reformation of the sector is performed in accordance with the planned schedule, and, if the collaboration of the Ukraine's central bank, commercial banks and customers is successfully implemented, there is a possibility that the banking industry will slowly start to recover already in 2016.

Generally positive is the fact that together with the restructuring of the national external debt, Ukraine has been able to postpone debt repayment period up to 2019 - 2027 and slightly reduced the debt amount. Decrease in refinancing needs and planned receipt of funding from creditors reduce the sovereign debt crisis risks in the short and medium term perspective.

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.

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, all of which have been applied consistently throughout 2015 and 2014, 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 Bank's financial position, access to financial resources and analysed the impact of the recent financial crisis on the future operations of 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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(b) Basis of preparation (continued)

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 2015 are consistent with those used in the annual financial statements for the year ended 31 December 2014, except as referred to in Note 3 (bb) *Adoption of New or Revised Standards and Interpretations.*

(c) 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.

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.

(d) Foreign currency translation

Functional and presentation currency

Items included in the financial statements of the Bank are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The financial statements are presented in euros ('EUR'), which is the Bank's functional and 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 balance sheet of the Bank, the following currency exchanges rates were most commonly used (EUR against foreign currency unit):

Reporting date	USD	*UAH
As at 31 December 2015	1.0887	24.8800
As at 31 December 2014	1.2141	19.2349

*Due to the fact that ECB does not publish UAH rate on its official website, the Bank uses Bloomberg L.P. currency rates.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(e) 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.

(f) 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.

(g) 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 repayments.

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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(g) Loans and provisions for loan impairment (continued)

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.

(h) 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.

(i) 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.

(j) 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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(k) 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.

(l) 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.

(m) 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.

(n) 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.

(o) 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.

(p) 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.

(q) 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. All other repairs and maintenance are charged to the statement of comprehensive income during the financial period in which they are incurred.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(q) Property and Equipment (continued)
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.

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.

(r) 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.

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

(t) 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.

(u) 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.

(v) 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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(w) 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 71,55% (2014: 73.80%) 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.

(x) 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 (t) of Note 3 above.

(y) 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.

(z) 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.

(aa) Critical accounting estimates

Loan impairment

The Bank reviews its loan portfolio to assess impairment on a regular basis. In determining whether an impairment loss should be recorded in the statement of comprehensive income, the Bank’s Management makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio.

This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

The Bank applies stress – tests in order to evaluate the impact of changes in one or a number of variables, which are used for determination of provisions for loan impairment losses, on the financial result. If overdue loans in loan portfolio increase by 1%, provisions for loan impairment losses would increase by EUR 497.74 thousand (in 2014: EUR 261 thousand).

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(aa) Critical accounting estimates (continued)

Securities valued at fair value
The Bank used quoted market prices to value securities carried at fair value as at year end for those securities which in the management's judgement are traded at liquid markets. The management had evaluated the liquidity of the securities market and has concluded that there is a significant reduction of activities in market, however, consider the market to be active with respect to type of securities held by the Bank therefore quoted market prices available on Stock Exchange of the security issuer countries were used to determine the fair values of the securities as at year end.

Initial recognition of related party transactions
In the normal course of business the Bank enters into transactions with its related parties. IAS 39 requires initial recognition of financial instruments based on their fair values. Management's judgement is applied in determining if transactions are priced at market or non-market interest rates, where there is no active market for such transactions. The basis for judgement is pricing for similar types of transactions with unrelated parties and effective interest rate analysis.

(bb) Adoption of new or revised standards and interpretations

The following new and amended IFRS and interpretations became effective in 2015, but have no significant impact on these financial statements:

Amendments to IAS 19 “Employee benefits plans” regarding defined benefit plans (effective for annual periods beginning on or after 1 July 2014, endorsed by EU for annual periods beginning on or after 1 February 2015);

Annual improvements 2012 (effective for annual periods beginning on or after 1 July 2014, by EU 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”;
- IAS 24 “Related party disclosures”.

Annual improvements 2013 (effective for annual periods beginning on or after 1 July 2014, endorsed by EU for annual periods beginning on or after 1 January 2015). The amendments include changes that affect 3 standards:
- IFRS 3 “Business combinations”;
- IFRS 13 “Fair value measurement”; and
- IAS 40 “Investment property”.

A number of new standards and interpretations have been published and come into force on financial periods beginning after 1 January 2015, or are not endorsed by the European Union:

IFRS 14 “Regulatory deferral accounts” (effective for annual periods beginning on or after 1 January 2016, not yet endorsed in the EU);

Amendment to IFRS 11 “Joint arrangements” on acquisition of an interest in a joint operation (effective for annual periods beginning on or after 1 January 2016, not yet endorsed in the EU);

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, not yet endorsed in the EU);

Amendment to IAS 16 “Property, plant and equipment” and IAS 38 “Intangible assets” on depreciation and amortisation (effective for annual periods beginning on or after 1 January 2016, not yet endorsed in the EU);

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(bb) Adoption of new or revised standards and interpretations (continued)

Amendments to IAS 27 “Separate financial statements” on the equity method (effective for annual periods beginning on or after 1 January 2016, not yet endorsed in the EU);

Amendments to IFRS 10 “Consolidated financial statements” and IAS 28 “Investments in associates and joint ventures” (effective for annual periods beginning on or after 1 January 2016, not yet endorsed in the EU);

Amendments to IAS 1 “Presentation of financial statements” regarding disclosure initiative effective for annual periods beginning on or after 1 January 2016, not yet endorsed in the EU). Adoption of these amendments will not influence valuation and accounting treatment of the financial statement line items, however, it will significantly impact the presentation and layout of the information disclosed within financial statements;

Annual improvements 2014 (effective for annual periods beginning on or after 1 January 2016, not yet endorsed in the EU). 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”;
• IAS 34 “Interim financial reporting”.

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

IFRS 9 “Financial instruments” (effective for annual periods beginning on or after 1 January 2018, not yet endorsed in the EU). 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.
The management of the Bank acknowledges the impact the new standard will have on the presentation and valuation of financial instruments, especially on the amount of impairment allowance for loans, however, detailed calculations have not been performed and the impact cannot be quantified so far.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(bb) Adoption of new or revised standards and interpretations (continued)

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

The Bank's management believes that adoption of new standards will not significantly affect the Bank's financial statements, except for the amendments to IAS 1 on disclosure initiative and implementation of IFRS 9.

(cc) Categories of financial instruments
Financial instruments held by the bank can be classified as Loans and receivables, Financial assets/ liabilities at fair value with revaluation through profit or loss, Available-for-sale financial assets and Other financial liabilities. Bank does not possess Held to maturity instruments. Financial instruments held by 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 with revaluation 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;
- Other financial liabilities are comprised of Balances due to banks, Customer accounts, Subordinated loan and Other financial liabilities.

NOTE 4 FINANCIAL RISK MANAGEMENT

Risk Management
Risk management is one of the 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 and residual 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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4 FINANCIAL RISK MANAGEMENT (continued)

(a) Credit risk (continued)

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 repayments 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.

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:

	31.12.2015. EUR	31.12.2014. EUR
Credit risk exposures relating to on-balance sheet assets are as follows:		
Balances on demand with the Bank of Latvia	113,537,989	100,081,040
Loans to banks	142,561,234	216,007,335
Loans to customers	67,784,042	70,395,363
Financial assets at fair value through profit or loss	288,969,771	199,934,383
Other assets	2,775,153	3,102,207
Total	**615,628,189**	**589,520,328**
Credit risk exposures relating to off-balance sheet items are as follows:		
Guarantees issued	10,725,694	4,694,429
Credit related commitments	24,536,046	26,892,521
Total	**35,261,740**	**31,586,950**

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.

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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4 FINANCIAL RISK MANAGEMENT (continued)

(a) Credit risk (continued)
Standard loans are loans, repayment 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 borrowing 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 2015 and 2014 the Bank was in compliance with those limits (see Note 25). Bank has no significant open positions in "exotic" currencies.

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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4 FINANCIAL RISK MANAGEMENT (continued)

(c) Currency risk (continued)
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):

31.12.2015.	Effect on profit/ loss and equity		31.12.2014.	Effect on profit/ loss and equity	
	+10%	-10%		+10%	-10%
USD	(50)	50	USD	(11)	11
Total	**(50)**	**50**	**Total**	**(11)**	**11**

(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 27).

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.

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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4 FINANCIAL RISK MANAGEMENT (continued)

(d) Interest rate risk (continued)
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):

31.12.2015.	Effect on profit/ loss and equity		31.12.2014.	Effect on profit/ loss and equity	
USD	(547)	547	**USD**	(347)	347
EUR	(54)	54	**EUR**	(188)	188
Total	**(601)**	**601**	**Total**	**(535)**	**535**

(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 26). 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.

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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4 FINANCIAL RISK MANAGEMENT (continued)

(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.

(f) Capital adequacy (continued)

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 2015 was 23.26 % (as at 31 December 2014 – 26.59%), 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 24). At the end of 2015 the Finance and Capital Markets Commission recalculated individual capital adequacy requirements placed on the Bank and determined it to be 15.6 %. The Bank observed and complied with the individually determined capital adequacy requirements both as at 31 December 2015 and 31 December 2014.

(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.

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.

OTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4 FINANCIAL RISK MANAGEMENT (continued)

(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

	2015 EUR	2014 EUR
Interest income		
Loans and advances to legal entities	4,798,204	4,973,101
Loans and advances to private individuals	133,089	163,405
Balances due from banks	2,040,044	5,505,355
Trading securities	1,322,193	612,305
Total interest income	**8,293,530**	**11,254,166**
Interest expense		
Due to private individuals	(679,048)	(766,938)
Due to legal entities	(2,202,066)	(2,151,329)
Subordinated loan	(1,067,257)	(892,492)
Other interest and related expenses	(1,441,611)	(1,064,402)
Total interest expense	**(5,389,982)**	**(4,875,161)**
Net interest income	**2,903,548**	**6,379,005**

Interest income from impaired loans amounts to EUR 1,754,748 (2014: EUR 1,332,410).

Other interest and related expenses include payments to the deposit guarantee fund EUR 749,625 (in 2014: 921,758 EUR), as well as payments to finance the FCMC 127,356 EUR (in 2014: 85,506 EUR), the financial stability fee of EUR 359,539 (in 2014 year: 1,330 EUR) and negative interest rate applied on correspondent accounts of EUR 205.091 (in 2014: 55,808 EUR).

NOTE 6 FEE AND COMMISSION INCOME AND EXPENSE

	2015 EUR	2014 EUR
Fee and commission income		
Money transfers	6,644,243	4,745,744
Fees on registration of changes in loan agreements	1,871	2,654
Commission income from asset management	168,445	439,520
Accounts servicing	945,970	572,381
Commissions from letters of credit	454,142	460,549
Commission income on transactions with securities	53,098	62,193
Commission income on current accounts servicing	136,938	81,317
Income from general services	63,978	34,169
Other commissions (DIGIPAS)	102,570	60,433
Interbank commission income	277,096	213,289
Commission for dealing with cards	231,309	197,443
Income from currency exchange	354,410	248,768
Other income	256,281	148,623
Total fee and commission income	**9,690,351**	**7,267,083**
Fee and commission expense		
Money transfers	(1,442,671)	(1,388,365)
Other expense	(41,154)	(29,814)
Total fee and commission expense	**(1,483,825)**	**(1,418,179)**
Net fee and commission income	**8,206,526**	**5,848,904**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 7 ADMINISTRATIVE EXPENSE

	2015 EUR	2014 EUR
Remuneration paid to personnel	3,277,413	2,836,371
Rent expense	130,363	402,527
Office and equipment maintenance	39,269	110,852
Remuneration paid to the members of the Council and the Board	446,486	408,256
Security services	2,100	2,873
Public utilities	101,301	51,830
State compulsory social insurance contributions	849,280	765,381
Communication expense	404,178	353,378
Consulting and professional fees	260,130	345,964
Set-up and maintenance costs of information systems	161,279	132,326
Business trips	89,393	101,587
Credit card expenses	-	4,324
Transportation	38,624	49,703
Health insurance	40,239	31,437
Advertising and marketing	17,254	15,210
Penalties	1	70,018
Other administrative expense	589,266	484,658
	6,446,576	**6,166,695**

The average number of staff employed by the Bank in 2015 was 159 (in 2014: 144).

NOTE 8 INCOME TAX EXPENSE

Corporate income tax for the reporting year	-	-
Amount of tax paid abroad	285,021	569,342
Deferred tax (see Note 19)	52,872	148
Total corporate income tax	**337,893**	**569,490**

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

Loss before income tax	**(1,231,914)**	**(1,312,750)**
Theoretically calculated tax at a tax rate of 15%	(184,787)	(196,913)
Loss from revaluation of securities at fair value through profit or loss	41,201	60,597
Other expenses not deductible for tax purposes	502,426	259,490
Non-taxable income and tax allowances	(305,969)	(123 026)
Amount of tax paid abroad	285,021	569,342
Corporate income tax expense	**337,893**	**569,490**

* Amount of tax withheld 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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 9 CASH AND BALANCES WITH THE BANK OF LATVIA

	31.12.2015. EUR	31.12.2014. EUR
Cash	909,526	1,225,468
Balances on demand with the Bank of Latvia	113,537,989	100,081,040
	114,447,515	**101,306,508**

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 09 December 2015 to 31 December 2015 was set at EUR 5,768,172 (in 2014: 4,594,256 EUR).

The Bank was in compliance with the reserve requirement of the Bank of Latvia during 2015 and 2014.

NOTE 10 BALANCES DUE FROM BANKS

	31.12.2015. EUR	31.12.2014. EUR
Due from Republic of Latvia credit institutions	21,468,113	20,023,153
Due from non-OECD credit institutions	52,218,409	81,126,500
Due from OECD credit institutions	68,972,595	114,857,682
Balances due from banks, gross	**142,659,117**	**216,007,335**
Provisions for impairment of balances due from banks	(97,883)	-
Balances due from banks, net	**142,561,234**	**216,007,335**

As at 31 December 2015 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:

On demand	98,648,930	176,466,586
Balances with maturity of three months or less	31,003,841	13,460,477
Other balances due from banks	13,006,346	26,080,272
Balances due from banks, gross	**142,659,117**	**216,007,335**
Provisions for impairment of balances due from banks	(97,883)	-
Balances due from banks, net	**142,561,234**	**216,007,335**

The following table discloses balances due from banks according to their ratings as at 31 December 2015 and 31 December 2014:

	31.12.2015.		**31.12.2014.**	
Rating	**Due from banks**		**Due from banks**	
	EUR	**%**	**EUR**	**%**
Aaa to Aa3	-	-	6,443,279	2,98%
A1 to A3	20,184,373	14.16%	80,349,664	37,20%
Baa1 to Baa3	61,109,415	42,87%	74,900,772	34,68%
Ba1 to Ba3	500,440	0.35%	1,286,097	0,60%
B1 to B3	14,700,488	10.31%	15,377,297	7.12%
Below B3	23,252,019	16.31%	27,052,377	12,52%
	119,746,735	**84.00%**	**205,409,486**	**95.09%**
Without rating	22,912,382	16.00%	10,597,849	4,91%
Provisions for impairment of balances due from banks	(97,883)	-	-	-
Balances due from banks, net	**142,561,234**	**100.00%**	**216,007,335**	**100,00%**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11 LOANS AND ADVANCES TO CUSTOMERS

Analysis of loans by client type and by products:

	31.12.2015. EUR	31.12.2014. EUR
Loans to legal entities	100,341,556	95,718,164
Loans to private individuals, except for mortgages	1,676,857	1,748,648
Mortgages	1,956,288	1,925,683
Gross loans and advances to customers	**103,974,701**	**99,392,495**
Less: provisions for loan impairment	(36,190,659)	(28,997,132)
Total loans and advances to customers	**67,784,042**	**70,395,363**

The following table discloses changes in provisions for loan impairment during 2015:

	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 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 following table discloses changes in provisions for loan impairment during 2014:

	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 2013	**17,466,817**	**1,630,046**	**603,969**	**19,700,832**
Increase in provisions for loan impairment for the year	6,913,034	(997)	609,653	7,521,689
Impact of foreign currency revaluation	1,696,750	-	77,860	1,774,610
Provisions for loan impairment as at 31 December 2014	**26,076,601**	**1,629,049**	**1,291,482**	**28,997,132**

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

	2015		2014	
	EUR	%	EUR	%
Trade and commercial activities	32,314,677	31.08	29,549,812	29.73
Private individuals	3,633,145	3,49	3,674,331	3.70
Agriculture and food industry	2,729,191	2.62	5,239,455	5.27
Construction and operations with real estate	28,098,792	27.02	26,026,470	26.19
Transport and communication	15,143,291	14.56	17,281,158	17.39
Industry	10,651,285	10.24	6,736,580	6.78
Tourism and hotel services, restaurant business	155,318	0.15	1,217,013	1.22
Financial services	4 066 598	3.91	4,145,199	4.17
Other	7,182,404	6.91	5,522,478	5.55
Loans and advances to customers (before provisions for impairment)	**103,974,701**	**100.00**	**99,392,495**	**100.00**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11 LOANS AND ADVANCES TO CUSTOMERS (continued)

As at 31 December 2015, the total amount of loans issued to 10 largest customers was EUR 45,880,708 (2014: EUR 50,840,154), which comprises 44.13 % of the total credit portfolio (2014: 51.15 %). As at 31 December 2015 loans to 10 largest customers were secured by deposits amounting to EUR 13,001,878 (31 December 2014: 7,829,909 EUR).

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
- cash 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**

The following table shows the information about collateral as at 31 December 2014:

	Loans to legal entities	Loans to private individuals, except for mortgages	Mortgages	Total
	EUR	**EUR**	**EUR**	**EUR**
Unsecured	10,060,244	1,745,684	323,168	**12,129,096**
Loans with sufficient collateral:				
- residential real estate	815,127	-	526,779	1,341,906
- other real estate	26,738,886	-	-	26,738,886
- cash deposits	3,656,615	1,316	-	3,657,931
- guarantees and other assets	17,058,188	-	-	17,058,188
Loans with insufficient collateral:				
- residential real estate	1,097,398	-	184,492	1,281,890
- other real estate	27,734,234	-	891,244	28,625,478
- cash deposits	4,798,176	1,648	-	4,799,824
- guarantees and other assets	3,759,297	-	-	3,759,297
Total loans and advances to customers (before provisions for impairment)	**95,718,164**	**1,748,648**	**1,925,683**	**99,392,495**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11 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 loans				
- 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 from 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 up to 30 days	217,846	-	-	**217,846**
- past due 91 – 180 days	1,433,609	-	-	**1,433,609**
- past due 181 – 360 days	4,946,105	-	-	**4,946,105**
- past due over 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**
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**

Loans past due, but not impaired include all amounts due from borrowers. Amount actually overdue as at 31 December 2015 was 21,881 EUR (as at 31 December 2014: 775,300 EUR).

Loans past due and individually impaired include all amounts due from borrowers. Amount actually overdue as at 31 December 2015 was 30,678,925 EUR (as at 31 December 2014: 30,197,658 EUR).

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11 LOANS AND ADVANCES TO CUSTOMERS (continued)

The following table shows the loans outstanding as at 31 December 2014 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	45,233,496	112,272	526,779	**45,872,547**
- Close control	-	-	-	**-**
- Substandard	277,047	-	-	**277,047**
Total neither past due nor impaired	**45,510,543**	**112,272**	**526,779**	**46,149,594**
Past due but not impaired				
- past due up to 30 days	479,713	-	-	**479,713**
- past due from 30 to 90 days	4,097,853	-	-	**4,097,853**
- past due from 91 to 180 days	271,147	-	-	**271,147**
- past due from 181 to 360 days	102,841	41	-	**102,882**
Total past due but not impaired	**4,951,554**	**41**	**-**	**4,951,595**
Individually impaired loans (total amount)				
- not past due	11,587,865	-	1,075,736	**12,663,601**
- past due 30 days	2,248,470	-	-	**2,248,470**
- past due from 30 to 90 days	50,612	-	-	**50,612**
- past due from 91 to 180 days	10,634,764	-	-	**10,634,764**
- past due 181 to 360 days	1,906,520	28,769	-	**1,935,289**
- past due over 360 days	18,827,836	1,607,566	323,168	**20,758,570**
Total individually impaired loans (total amount)	**45,256,067**	**1,636,335**	**1,398,904**	**48,291,306**
Less: provisions for loan impairment	**(26,076,601)**	**(1,629,049)**	**(1,291,482)**	**(28,997,132)**
Net loans and advances to customers	**69,641,563**	**119,599**	**634,201**	**70,395,363**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11 LOANS AND ADVANCES TO CUSTOMERS (continued)

The recoverable 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 EUR	Mortgages EUR
Recoverable 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	-
Recoverable 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 recoverable 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 2014 was as follows:

	Loans to legal entities EUR	Mortgages EUR
Recoverable value of collateral – loans past due but not impaired		
- Residential real estate	1,403,037	-
- Other real estate objects	41,711,167	-
- deposits	3,226,159	-
- Other assets	9,004,424	-
Recoverable value of collateral – individually impaired loans		
- Residential real estate	649,149	107,574
- Other real estate objects	15,792,916	-
- deposits	4,798,176	-
- Other assets	108,803	-
Total	**76,693,831**	**107,574**

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 11 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 “Recoverable 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 may impact the expenses for foreclosure and sale of collateral as well as the sales price of the collateral.

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) EUR	**Recoverable value of collateral EUR**	**Book value of asset (before provisions for impairment) EUR**	**Recoverable value of collateral 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**

The impact of collateral at 31 December 2014:

	Assets with collateral value exceeding the loan balance		**Assets with insufficient collateral**	
	Book value of asset (before provisions for impairment) EUR	**Recoverable value of collateral EUR**	**Book value of asset (before provisions for impairment) EUR**	**Recoverable value of collateral EUR**
Loans to legal entities	48,268,816	141,515,281	47,449,347	21,349,044
Loans to individuals – consumer loans	1,316	66,292	1,747,332	1,647
Mortgage loans	526,779	1,088,814	1,398,904	107,574
Total	**48,796,911**	**142,670,387**	**50,595, 583**	**21,458,265**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 12 FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

	31.12.2015. EUR	31.12.2014. EUR
Latvian government debt securities	19,381,188	17,817,963
OECD state government debt securities	241,302,647	173,552,232
Non-OECD state government debt securities	9,917,633	8,506,507
Non-OECD region corporate debt securities	9,236,577	-
Unquoted shares	9,131,726	57,681
Quoted shares	8,212	7,364
	288,977,983	**199,941,747**

The following table discloses securities by issuers' ratings as at 31 December 2015 and 31 December 2014:

Rating	31.12.2015. Securities EUR	31.12.2015. %	31.12.2014. Securities EUR	31.12.2014. %
Aaa to Aa3	228,478,374	79.06%	160,594,154	80,32%
From A1 to A3	38,990,713	13.49%	8,533,417	4,27%
From Baa1 to Baa3	12,368,958	4.28%	30,749,130	15,38%
From Ba1 to Ba3	9,098,390	3.15%	-	-
From B1 to B3	-	-	28,030	0,01%
Below B3	41,548	0.02%	7,364	0,00%
	288,977,983	100.00%	**199,912,095**	99.98%
Without rating	-	-	29,652	0.02%
	288,977,983	**100%**	**199,941,747**	**100%**

NOTE 13 INTANGIBLE ASSETS

The following changes in the Bank's intangible assets took place during 2015 and 2014:

	Software 2015 EUR	Software 2014 EUR
Cost		
As at the beginning of the year	**1,492,506**	**1,377,496**
Additions	96,249	115,010
As at end of the year	**1,588,755**	**1,492,506**
Amortisation		
Accumulated amortisation at the beginning of the year	**1,255,427**	**1,145,986**
Charge for the year	78,010	109,441
Accumulated amortisation at the end of the year	**1,333,437**	**1,255,427**
Net book value at the beginning of the year	**237,079**	**231,510**
Net book value at the end of the year	**255,318**	**237,079**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 14 PROPERTY AND EQUIPMENT

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

	Land and building	Transport	Computers	Office equipment	Other fixed assets	Total
		EUR	EUR	EUR	EUR	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".

The following changes in the Bank's property and equipment took place during the year ended 31 December 2014:

	Transport	Computers	Office equipment	Leasehold improvements	Total
	EUR	EUR	EUR	EUR	EUR
Cost					
31.12.2013.	**61,455**	**711,535**	**593,039**	**100,927**	**1,466,956**
Additions	27,557	44,160	20,177	-	91,894
Disposals	-	(33,903)	(29,317)	-	(63,220)
31.12.2014.	**89,012**	**721,792**	**583,899**	**100,927**	**1,495,630**
Depreciation					
31.12.2013.	**25,087**	**646,893**	**490,225**	**30,584**	**1,192,789**
On disposals	**-**	(33,911)	(17,305)	**-**	(51,216)
Charge for 2014	8,902	45,768	27,104	6,115	87,889
31.12.2014.	**33,989**	**658,750**	**500,024**	**36,699**	**1,229,462**
Net book value 31.12.2013.	**36,368**	**64,642**	**102,814**	**70,343**	**274,167**
Net book value 31.12.2014.	**55,023**	**63,042**	**83,875**	**64,228**	**266,168**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 15 CUSTOMER ACCOUNTS

(a) Analysis of groups by customers

	31.12.2015. EUR	31.12.2014. EUR
Legal entities		
- current/ settlement accounts	481,454,379	472,830,037
- term deposits	35,934,617	12,215,905
Private individuals		
- current/ settlement accounts	49,863,865	38,092,339
- term deposits	16,726,929	17,794,882
Total customer accounts:	**583,979,790**	**540,933,163**
Sector profile:		
Private companies	517,340,044	484,657,024
Private individuals	66,590,794	55,887,221
Financial institutions	6	243,050
Non-profit institutions	32,821	137,185
Latvian government	16,125	8,683
Total customer accounts:	**583,979,790**	**540,933,163**

(b) Analysis by place of residence

Residents	26,786,289	23,512,866
Non-residents	557,193,501	517,420,297
Total customer accounts:	**583,979,790**	**540,933,163**

The average interest rate on term deposits in 2015 was 2.68 % (2014: 4.02%) and the average interest rate on demand deposits was 0,04% (2014: 0.16%). All deposits have a fixed interest rate.

Economic sector concentration within customer accounts is as follows:

	2015		2014	
	EUR	**%**	**EUR**	**%**
Manufacturing	6,187,973	1.06	4,692,483	0.87
Building and real estate	20,285,064	3.47	7,847,147	1.45
Trade and commercial activities	281,292,693	48.17	278,737,231	51.53
Financial and insurance services	109,951,416	18.,83	77,646,401	14.35
Transport and communications	90,986,483	15.58	98,964,618	18.30
Agriculture and food industries	791,499	0.14	3,154,595	0.58
Private individuals	66,590,794	11.40	55,887,221	10.37
Other	7,893,868	1.35	14,003,468	2.57
Total customer accounts	**583,979,790**	**100,00**	**540,933,163**	**100,00**

Amount attributable to 20 largest depositors as at 31 December 2015 is EUR 200,499,793 (in 2014: EUR 210,219,654), comprising 34.33% of the total portfolio (in 2014: 38,86%).

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 16 BALANCES DUE TO BANKS

	31.12.2015. EUR	31.12.2014. EUR
Other interbank borrowings	**-**	**7,365**

NOTE 17 OTHER FINANCIAL LIABILITIES

	31.12.2015. EUR	31.12.2014. EUR
Liabilities in clearance	454,042	2,054,024
Settlements on behalf of a closed bank	16,585	16,585
Cash in transit	69,358	124,219
Creditors settlements	195,139	150,712
	735,124	**2,345,540**

Liabilities in clearance as at 31 December 2015 and 31 December 2014 include amounts erroneously transferred to the Bank, which were returned to senders at the beginning of 2016 and 2015 respectively.

NOTE 18 DEFERRED INCOME AND ACCRUED EXPENSES

	31.12.2015. EUR	31.12.2014. EUR
Accrued annual leave expenses	260,544	197,652
Accrual for guarantee fund and FCMC financing	469,478	290,717
State social security contributions to be paid	151,166	125,148
Accrued commission expenses	132,182	222,047
Other accrued expenses	123,255	39,210
	1,136,625	**874,774**

NOTE 19 DEFERRED INCOME TAX

Deferred income tax is calculated by using the enacted tax rate – 15%.

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

	2015 EUR	2014 EUR
Deferred income tax asset at the beginning of the reporting year	(19,163)	(19,311)
Deferred income tax change during the reporting year (see Note 8)	52,872	148
Deferred tax liability/ (asset) at the end of the reporting year	**33,709**	**(19,163)**

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:

	31.12.2015. EUR	31.12.2014. EUR
Deferred income tax liability:		
Temporary difference on fixed assets depreciation	135,849	17,784
Deferred income tax assets:		
Temporary difference on accruals for unused annual leave	(48,764)	(36,947)
Temporary difference on accrual financial stability fee	(53,375)	-
Deferred tax liability/ (asset)	**33,709**	**(19,163)**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 20 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.

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

	31.12.2015.			31.12.2014.		
	Contract/ national amount	Fair value		Contract/ national amount	Fair value	
		Assets	Liabilities		Assets	Liabilities
	EUR	EUR	EUR	EUR	EUR	EUR
Currency swaps	84,202,810	237,623	(1,042,200)	43,539,914	736,418	(514,290)
Currency forwards	18,645,198	25,112	(67,243)	750,195	194	(1,134)
Total	**102,848,008**	**262,735**	**(1,109,443)**	**44,290,109**	**736,612**	**(515,424)**

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

	31.12.2015.			31.12.2014.		
Rating	Contract/ national amount	Fair value		Contract/ national amount	Fair value	
		Assets	Liabilities		Assets	Liabilities
	EUR	EUR	EUR	EUR	EUR	EUR
Aaa to Aa3	3,282,674	5,456	(4,720)	750,195	195	(1,134)
A1 to A3	40,149,444	149,444	(122,440)	-	-	-
Baa to Baa3	-	-	-	20,388,271	386,333	-
B1 to B3	39,088,179	88,179	(64,572)	19,351,643	348,248	-
Caa1 and below	12,049,600	-	(49,600)	-	-	-
Without rating	8,278,111	19,656	(868,111)	3,800,000	1,836	(514,290)
Total	**102,848,008**	**262,735**	**(1,109,443)**	**44,290,109**	**736,612**	**(515,424)**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 21 SHARE CAPITAL

Issued and fully paid share capital as at 31 December 2015 was EUR 32,334,762 (31 December 2014: EUR 32,334,762). Nominal value of one share is EUR 1.43 (31 December 2014: EUR 1.43). All shares are ordinary equity shares with voting rights.

During 2015 the following changes were made in the composition of the shareholders of the Bank:

During March 2015 shareholder of the Bank AB "Pivdenny" sold 1 136 250 of its shares to Jurij Rodin.

During June 2015 shareholder of the Bank Irina Veseluh sold all of its 25 000 shares to Mark Bekker.

During August 2015 shareholder of the Bank OOO "Portfolio Investor" sold all of its 430 100 shares and shareholder of the Bank OOO "Winster" sold all of its shares 358 400 to DrawNex Universal S.A.

During October 2015 shareholder of the Bank DrawNex Universal S.A. sold all of its 430 100 shares to OOO "Portfolio Investor".

During March 2015 shareholder of the Bank AB "Pivdenny" sold 8 500 0000 of its shares to JSC "SKY Investment Holding".

During December 2015 Bank shareholder DrawNex Universal S. A. sold all of its 358 400 shares to OOO "Winster" and the shareholder of the Bank OOO "Winster" sold all of its 358 400 shares to PAS „Zakritij nediversificirovannij venčurnij korporativnij investicionnij fond "Strategičeskije investiciji"".

As at 31 December 2015 and 31 December 2014 shareholders of the Bank were:

	31.12.2015.		31.12.2014.	
	Paid-in share capital	% of total paid-in capital	Paid-in share capital	% of total paid-in capital
	EUR	%	EUR	%
"SKY Investment Holding" LLC	12,094,410	37.40	-	-
Jurij Rodin	6,466,198	20.00	4,849,460	15.00
AB „Pivdenny" bank	4,772,910	14.76	18,484,058	57.16
Mark Bekker	3,095,458	9.57	3,059,886	9.46
"Jasnii Zori" OOO	1,937,952	6.00	1,937,952	6.00
DrawNex Universal S.A	1,565,159	4.84	1,565,159	4.84
Aztin corporation	711,436	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	-	-
"Winster" OOO	-	-	509,957	1.58
Olegs Atayants	284,574	0.88	284,574	0.88
Vitalijs Medvedcuks	284,574	0.88	284,574	0.88
Irina Veseluha	-	-	35,572	0.11
Daiga Muravska	157	-	157	-
	32,334,762	**100.00**	**32,334,762**	**100.00**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 22 OFF-BALANCE SHEET POSITIONS AND PLEDGED ASSETS

Guarantees

The following table discloses guarantees issued:

	31.12.2015. EUR	31.12.2014. EUR
Financial guarantees	10,725,694	4,694,429
	10,725,694	**4,694,429**

The Bank has issued financial guarantees in the amount of EUR 10,725,694. These guarantees are secured by deposits placed with the Bank or money resources in the security accounts or insurance policy of an insurance company.

Off-balance sheet credit related commitments

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

	31.12.2015. EUR	31.12.2014. EUR
Letters of credit	-	21,815
Lending commitments	24,536,046	26,870,706
	24,536,046	**26,892,521**

From which Bank’s commitments relating to lending were as follows:

	31.12.2015. EUR	31.12.2014. EUR
Loan commitments	7,661,902	5,330,541
Undrawn credit lines	16,874,144	21,540,165
Total lending commitments	**24,536,046**	**26,870,706**

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

The loan commitments are denominated in the following currencies:

	31.12.2015. EUR	31.12.2014. EUR
USD	6,899,614	2,988,477
EUR	762,288	2,342,064
Total	**7,661,902**	**5,330,541**

The undrawn credit lines are denominated in the following currencies

	31.12.2015. EUR	31.12.2014. EUR
USD	9,204,102	13,808,047
EUR	7,670,042	7,732,118
Total	**16,874,144**	**21,540,165**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 22 OFF-BALANCE SHEET POSITIONS AND PLEDGED ASSETS

Assets pledged and restricted

As at year 2015 and 2014 the Bank had the following assets pledged:

	2015	2014
	Assets pledged EUR	Assets pledged EUR
Balances due from banks	18,257,571	6,814,011
Other assets	695,613	634,610
Total	**18,953,184**	**7,448,621**

All encumbered assets serve as a pledge for liabilities of the Bank as at 31 December 2015 and 31 December 2014.

Carrying value of encumbered assets approximates their fair value both as at 31 December 2015 and as at 31 December 2014.

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.

Encumbered assets of the Bank as at 31 December 2014 are comprised of the following assets:
- EUR 634,610 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 4,095,948 security deposits for guarantees issued by the Bank. Total amount of these encumbered assets is included within balances due from other banks.
- EUR 2,718,063 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.

NOTE 23 CASH AND CASH EQUIVALENTS

	31.12.2015. EUR	31.12.2014. EUR
Cash and balances on demand with the Bank of Latvia	114,447,515	101,306,508
Due from banks with original maturity of 3 months or less	129,554,888	189,927,063
Due to banks with original maturity of 3 months or less	-	(7,365)
	244,002,403	**291,226,206**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 24 CAPITAL ADEQUACY

The Bank’s calculation of the capital adequacy ratio according to the Finance and Capital Market Commission Guidelines as at 31 December 2015 and 31 December 2014 have been set in the table below:

Description	31.12.2015. EUR	31.12.2014. EUR
Total own funds	**45,673,236**	**47,024,138**
- Tier 1 capital	33,781,198	35,369,244
- Common equity Tier 1 capital	33,781,198	35,369,244
- Tier 2 capital	11,892,038	11,654,894
Total risk exposure amount	**196,376,490**	**176,827,836**
- Risk weighted exposure amounts for credit, counterparty credit and dilution risks and free deliveries	137,288,426	141,495,348
- Total risk exposure amount for position, foreign exchange and commodities risks	30,777,976	10,897,100
- Total risk exposure amount for operational risk	28,310,088	24,435,388
Capital adequacy ratios		
- Common equity Tier 1 Capital ratio	17.20%	20.00%
- Surplus (+) / Deficit (-) of Common equity Tier 1 capital (4.5%)	24,944,256	27,411,991
- Tier 1 Capital ratio	17.20%	20.00%
- Surplus (+) / Deficit (-) of Tier 1 capital (6%)	21,998,609	24,759,574
- Total capital ratio	23.26%	26.59%
- Surplus (+) / Deficit (-) of total capital (8%)	29,963,117	32,877,911
- Total capital ratio	23.26%	26.59%
- Surplus (+) / Deficit (-) of total capital (13.1% (in 2014 11%), calculated as a total individual capital requirement set to the Bank of 15.6% (in 2014 13.5%) less capital retention reserve of 2.5%)	19,947,916	27,573,076
- Capital retention reserve (%)	2.5%	2.5%
- Capital retention reserve	4,909,412	4,420,696

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 25 CURRENCY ANALYSIS

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 2015 by currency profile:

	USD EUR	EUR EUR	Other EUR	Total EUR
Assets				
Cash and deposits with the Bank of Latvia	232,639	114,214,704	172	114,447,515
Balances due from banks	119,656,874	6,890,316	16,014,044	142,561,234
Loans and advances to customers	35,991,971	31,792,071	-	67,784,042
Financial assets at fair value through profit or loss	279,372,421	9,605,562	-	288,977,983
Available-for-sale financial assets	-	919,980	-	919,980
Intangible assets	-	255,318	-	255,318
Property and equipment	-	14,902,365	-	14,902,365
Derivative financial instruments	-	262,735	-	262,735
Deferred expenses	43,300	106,557	1,011	150,868
Other assets	1,244,696	2,895,998	1,172,370	5,313,064
Total assets	**436,541,901**	**181,845,606**	**17,187,597**	**635,575,104**
Liabilities and equity				
Balances due to banks	-	-	-	-
Customer accounts	480,764,281	87,678,336	15,537,173	583,979,790
Derivative financial instruments	-	1,109,443	-	1,109,443
Deferred income and accrued expenses	183,642	920,871	32,112	1,136,625
Deferred tax liability	-	33,709	-	33,709
Other liabilities	475,909	259,215	-	735,124
Subordinated loan	13,623,927	-	-	13,623,927
Equity	-	34,956,486	-	34,956,486
Total liabilities and 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**	**(3,202,395)**	**1,890,751**	**(846,708)**
As at 31 December 2014				
Total assets	**427,977,378**	**158,815,350**	**5,706,621**	**592,499,349**
Total liabilities and shareholders' equity	**462,925,232**	**125,841,349**	**3,732,768**	**592,499,350**
Net long / (short) position on balance sheet	**(34,947,854)**	**32,974,001**	**1,973,853**	**-**
Off-balance sheet claims arising from foreign exchange				
Balances due from foreign exchange	39,940,108	4,350,000	-	44,290,108
Liabilities from foreign exchange	4,864,460	39,200,000	-	44,064,460
Net long / (short) position on foreign exchange	**35,075,648**	**(34,850,000)**	**-**	**225,648**
Net long / (short) position	***127,794***	***(1,875,999)***	***1,973,853***	***225,648***

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 26 LIQUIDITY RISK AND ANALYSIS OF ASSETS AND LIABILITIES BY MATURITY PROFILE

The table below allocates the Bank's assets and liabilities to maturity groupings as at 31 December 2015 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	-	114,447,515	-	-	-	-	-	**114,447,515**
Balances due from banks	-	129,554,889	31,452	1,952,573	11,022,320	-	-	**142,561,234**
Loans and advances to customers	9,658,048	4,850,354	6,586,192	5,111,658	21,197,507	19,355,639	1,024,644	**67,784,042**
Financial assets at fair value through profit or loss	-	184,432,792	18,327,830	9,239,405	20,463,164	55,059,391	1,455,401	**288,977,983**
Available-for-sale financial assets	-	-	-	-	-	-	919,980	**919,980**
Intangible assets	-	-	-	-	-	-	255,318	**255,318**
Property and equipment	-	-	-	-	-	-	14,902,365	**14,902,365**
Derivative financial instruments	-	262,735	-	-	-	-	-	**262,735**
Deferred expenses	-	-	-	-	150,868	-	-	**150,868**
Other assets	92,026	1,456,607	47,887	69,240	405,910	2,545,781	695,613	**5,313,064**
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**
Liabilities and equity								
Customer accounts	-	540,016,322	5,392,004	3,767,701	20,264,273	14,468,299	71,191	**583,979,790**
Derivative financial instruments	-	1,083,106	16,444	9,893	-	-	-	**1,109,443**
Deferred income and accrued expenses	-	680,821	27,923	102,789	325,092	-	-	**1,136,625**
Deferred tax liability	-	-	-	-	33,709	-	-	**33,709**
Other liabilities	-	735,124	-	-	-	-	-	**735,124**
Subordinated loan	-	5,850	-	-	-	7,647,654	5,970,423	**13,623,927**
Equity	-	-	-	-	-	-	34,956,486	**34,956,486**
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 26 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 2014								
Total assets	**10,879,005**	**466,592,224**	**21,563,005**	**14,563,449**	**26,918,251**	**45,446,321**	**6,537,094**	**592,499,349**
Total liabilities and equity	**-**	**502,425,324**	**8,333,243**	**5,825,456**	**16,124,543**	**16,019,868**	**43,770,915**	**592,499,349**
Off-balance sheet liabilities	**-**	**14,449,869**	**2,411,736**	**9,250,136**	**2,765,122**	**2,248,297**	**461,790**	**31,586,950**
Net liquidity	**10,879,005**	**(50,282,969)**	**10,818,026**	**(512,143)**	**8,028,586**	**27,178,156**	**(37,695,611)**	**(31,586,950)**

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 was 90.42 % (as at 31 December 2014: 91.06%) 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 2015:

	Overdue EUR	1 m. EUR	1-3 m. EUR	3-6 m. EUR	6-12 m. EUR	1-5 years EUR	Over 5 years and undated 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	**-**	**540,947,954**	**5,753,386**	**4,259,658**	**21,678,962**	**26,225,411**	**6,239,254**	**605,104,625**
Off-balance sheet liabilities	**-**	**2,122,398**	**3,620,948**	**8,516,857**	**10,769,332**	**10,050,724**	**181,481**	**35,261,740**

The table below allocates the Bank’s financial liabilities on undiscounted cash flow bases as at 31 December 2014:

	Overdue EUR	1 m. EUR	1-3 m. EUR	3-6 m. EUR	6-12 m. EUR	1-5 years EUR	Over 5 years and undated EUR	Total EUR
Balances due to banks	-	7,365	-	-	-	-	-	7,365
Customer accounts	-	499,270,917	8,389,692	5,872,866	16,126,399	12,287,028	72,564	542,019,466
Other liabilities	-	2,345,540	-	-	-	-	-	2,345,540
Subordinated loan	-	30,641	50,792	76,188	152,376	5,139,930	8,093,238	13,543,165
Total liabilities	**-**	**501,654,463**	**8,440,484**	**5,949,054**	**16,278,775**	**17,426,958**	**8,165,802**	**557,915,536**
Off-balance sheet liabilities	**-**	**14,449,869**	**2,411,736**	**9,250,136**	**2,765,122**	**2,248,297**	**461,790**	**31,586,950**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 26 LIQUIDITY RISK AND ANALYSIS OF ASSETS AND LIABILITIES BY MATURITY PROFILE (continued)

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

	Up to 1 month EUR	1 to 3 months EUR	Over 3 months EUR	Total 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**

The table below allocates the Bank's derivative instruments future cash flows as at 31 December 2014:

	Up to 1 month EUR	1 to 3 months EUR	Over 3 months EUR	Total EUR
Derivatives settled on a gross basis				
Foreign exchange derivatives:				
- inflow	44,290,109	-	-	44,290,109
- outflow	(44,064,460)	-	-	(44,064,460)

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 27 RE-PRICING MATURITY OF ASSETS AND LIABILITIES

The table below allocates the Bank's assets and liabilities to maturity groupings as at 31 December 2015 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	113,537,989	-	-	-	-	-	909,526	**114,447,515**
Balances due from banks	128,734,251	-	-	-	-	-	13,826,983	**142,561,234**
Loans and advances to customers	19,234,598	18,880,601	6,701,221	13,997,204	8,869,283	-	101,135	**67,784,042**
Financial assets at fair value through profit or loss	184,432,792	18,327,830	9,239,405	20,463,164	55,059,391	1,447,189	8,212	**288,977,983**
Available-for-sale financial assets	-	-	-	-	-	-	919,980	**919,980**
Intangible assets	-	-	-	-	-	-	255,318	**255,318**
Property and equipment	-	-	-	-	-	-	14,902,365	**14,902,365**
Other assets	-	-	-	-	-	-	5,726,667	**5,726,667**
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**
Liabilities and equity								
Customer accounts	8,591,609	5,365,847	1,806,006	9,133,498	14,259,171	71,144	544,752,515	**583,979,790**
Deferred tax liabilities	-	-	-	-	-	-	33,709	**33,709**
Other liabilities	-	-	-	-	-	-	2,981,192	**2,981,192**
Subordinated loan	-	-	-	-	7,647,653	5,970,424	5,850	**13,623,927**
Total liabilities	**8,591,609**	**5,365,847**	**1,806,006**	**9,133,498**	**21,906,824**	**6,041,568**	**547,773,266**	**600,618,618**
Equity	**-**	**-**	**-**	**-**	**-**	**-**	34,956,486	**34,956,486**
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)***	-
As at 31 December 2014								
Total assets	**372,482,244**	**26,607,442**	**9,020,638**	**16,694,249**	**36,118,867**	**4,899,678**	**126,915,431**	**592,499,349**
Total liabilities and equity	**14,653,519**	**4,588,971**	**1,578,782**	**4,687,603**	**15,580,600**	**8,164,381**	**543,245,493**	**592,499,349**
On balance sheet interest sensitivity analysis	*357,828,725*	*22,018,471*	*7,441,856*	*12,006,646*	*20,538,267*	*(3,264,703)*	*(416,569,262)*	-

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 28 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 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 28 RELATED PARTY TRANSACTIONS (continued)

Operations with the related parties were as follows as at 31 December 2014:

	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%)	22,873,259	2,861,818	5,033
Correspondent account	4,160,448	-	-
Customer accounts (interest rate: 0.10-5,0%)	-	5,287,968	25,381
Subordinate loan (interest rate on agreement: 8.0-8.5%)	8,095,074	823,816	-

Income and expense from operations with related parties during 2014 were as follows:

	Parent company of the Bank	Entities under control of the Bank's shareholders	Other related parties
Interest income	2,898,016	210,982	722
Interest expenses	613,615	399,512	31,644
Fee and commission income	-	232,321	790
Fee and commission expense	19,461	-	-
Administrative and other operating expenses	17,032	-	-

The balances in respect of off-balance sheet liabilities towards related parties are as follows as at 31 December 2014:

	Entities under control of the Bank's shareholders	Other related parties
Undrawn credit lines	82	3,809
Assets under management	6,823,458	-

Total amounts of loans issued to and repaid by related parties during 2014 are as follows:

	Parent company of the Bank	Entities under control of the Bank's shareholders	Other related parties
Issued to related parties	3,742,645,376	-	348,937
Repaid by related parties	3,777,552,866	-	352,852

Transactions with the parent company of the Bank include total amount of short term loans issued and repaid during 2014.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 28 RELATED PARTY TRANSACTIONS (continued)

Remuneration to key management personnel is disclosed below:

	2015 EUR	2014 EUR
Short-term benefits:		
- Salaries	432,040	444,686
Pension benefits:		
- Expenses to the State Pension Insurance	69,695	63,850
Total	**501,735**	**508,536**

NOTE 29 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, 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 29 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 (refer also to Note 34).

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.

The table below shows assets and liabilities valued at amortised cost by book values and fair values as at 31 December 2015 and 31 December 2014:

		31.12.2015.		31.12.2014.
	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	114,447,515	114,447,515	101,306,508	101,306,508
Balances due from Banks	142,561,234	142,561,234	216,007,335	216,007,335
Loans to legal entities	67,187,019	72,716,981	69,641,563	76,110,211
Loans to private individuals, except for mortgages	42,797	47,068	119,599	138,884
Mortgages	554,226	683,019	634,201	760,721
Other financial assets	2,775,153	2,775,153	3,102,207	3,102,207
Total assets valued at amortised cost	**327,567,944**	**333,230,970**	**390,811,413**	**397,425,866**
Liabilities valued at amortised cost				
Balances due to banks	-	-	7,365	7,365
Due to customers	583,979,790	585,474,321	540,933,163	541,468,909
Subordinated loan	13,623,927	13,621,367	12,216,760	12,078,809
Other financial liabilities	735,124	735,124	2,345,540	2,345,540
Total liabilities valued at amortised cost	**598,338,841**	**599,830,812**	**555,502,828**	**555,900,623**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 29 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES (continued)

The table below specified analysis by fair value levels as at 31 December 2015 and 31 December 2014 (based on carrying amounts):

	31.12.2015.			31.12.2014.		
	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	-	262,735	-	-	736,612	-
Available-for-sale financial assets	-	-	919,980	-	-	-
Financial assets at fair value through profit or loss	288,977,983	-	-	199,941,747	-	-
Total assets valued at fair value	**288,977,983**	**262,735**	**919,980**	**199,941,747**	**736,612**	**-**
Assets valued at amortised cost						
Cash and balances with the Bank of Latvia	-	114,447,515	-	-	101,306,508	-
Balances due from banks	-	142,561,234	-	-	216,007,335	-
Loans and advances to customers	-	-	67,784,042	-	-	70,395,363
Other financial assets	-	2,775,153	-	-	3,102,207	-
Total assets valued at amortised cost	**-**	**259,783,902**	**67,784,042**	**-**	**320,416,050**	**70,395,363**
Liabilities valued at fair value						
Derivative financial instruments	-	1,109,443	-	-	515,424	-
Total liabilities valued at fair value	**-**	**1,109,443**	**-**	**-**	**515,424**	**-**
Liabilities valued at amortised cost						
Balances due to banks	-	-	-	-	7,365	-
Customer accounts	-	583,979,790	-	-	540,933,163	-
Subordinated loan	-	-	13,623,927	-	-	12,216,760
Other financial liabilities	-	735,124	-	-	2,345,540	-
Total liabilities valued at amortised cost	**-**	**584,714,914**	**13,623,927**	**-**	**543,286,068**	**12,216,760**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 30 TAXES

	Balance as at 31.12.2014. EUR	Calculated in 2015 EUR	Returned from the budget EUR	Paid in 2015 EUR	Balance as at 31.12.2015. EUR
Corporate income tax*	-	285,021	-	(285,021)	-
State compulsory social insurance contributions	75,942	1,073,785	-	(1,063,060)	86,617
Personal income tax	-	618,818	-	(618,818)	-
Value added tax	13,205	36,960	10,178	(64,165)	(3,822)
(Overpaid)	**-**				**(3,822)**
Liabilities	**89,147**				**86,617**

* CIT calculated and paid includes the amount of tax withheld abroad – 285,021 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.

NOTE 31 SUBORDINATED LOAN

On 23 August 2011 the Bank signed an agreement with Venture Resource Investments LTD receiving subordinated loan in amount of USD 2,000,000 maturing in 2019. Interest rate for subordinated loan is 8%.

On 9 December 2011 the Bank signed an agreement with Aleksey Fedorichev receiving subordinated loan in amount of USD 2,000,000 maturing in 2018. Interest rate for subordinated loan is 7%.

On 8 June 2012 the Bank signed an agreement with Fortum Trade Services LTD receiving subordinated loan in amount of USD 1,000,000 maturing in 2019. Interest rate for subordinated loan is 7%.

On 20 June 2012 Bank signed an agreement with Pivdennyi Bank receiving subordinated loan in amount of USD 2,000,000, on 15 August – USD 5,000,000 and on 7 September – USD 5,500,000. On 11 December 2012 after receiving of approval from FCMC the agreements for subordinated loan in amounts of USD 2,000,000, USD 5,000,000 and USD 2,174,000 (part of USD 5,500,000) were cancelled and the assets were used in the increase of the Bank’s share capital for the amount LVL 5,000,000. During August 2015 Pivdenny Bank on a basis of cession agreement sold part of the subordinated debt (USD 1,000,000) to Fortum trade services LTD. As at 31 December 2015 the balance of the subordinated loan of Pivdenny Bank comprise USD 2,326,000. Maturity term is up to 2020. Interest rate for subordinated loan is 8.5%.

During August 2015 Fortum Trade Services LTD on a basis of cession agreement sold part (USD 420,000) of the subordinated debt of USD 1,000,000 to Igor Chudenkov. As at 31 December 2015 the balance of the subordinated loan of Igor Chudenkov comprise USD 420,000. Maturity term is up to 2020. Interest rate for subordinated loan is 8.5%.

During October 2015 Fortum Trade Services LTD on a basis of cession agreement sold part (USD 424,194) of the subordinated debt of USD 580,000 to MAXIPLAN L.P. As at 31 December 2015 the balance of the subordinated loan of MAXIPLAN L.P comprise USD 424,194. Maturity term is up to 2020. Interest rate for subordinated loan is 8.5%.

As at 31 December 2015 the balance of the subordinated loan of Fortum Trade Services LTD comprise USD 155,806. Maturity term is up to 2020. Interest rate for subordinated loan is 8.5%.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 31 SUBORDINATED LOAN (continued)

On 30 April 2013 the Bank signed an agreement with Pivdennyi Bank receiving subordinated loan in amount of USD 1,000,000 maturing in 2021. Interest rate for subordinated loan is 8.0%.

On 22 may 2013 the Bank signed an agreement with Pivdennyi Bank receiving subordinated loan in amount of USD 1,500,000 maturing in 2021. Interest rate for subordinated loan is 8.0%.

On 5 June 2013, Bank signed an agreement with the Bank on a subordinated loan Pivdenny receipt of USD 4,000,000 maturing in 2021. Interest rate for subordinated loan is 8.0%.

As at 31 December 2015 subordinated loans amounted to total of EUR 13,623,927 (31.12.2014: EUR 12,216,760).

NOTE 32 OTHER ASSETS

The following table represents split of other assets into financial and non-financial assets as at 31 December 2015 and 31 December 2014:

	31.12.2015. EUR	**31.12.2014. EUR**
Financial assets	2,855,860	3,102,207
Non-financial assets (repossessed collaterals)	2,537,911	332,343
Total other assets, gross	**5,393,771**	**3,434,550**
Provisions for impairment of other financial assets	(80,707)	-
Total other assets, net	**5,313,064**	**3,434,550**

Repossessed collaterals are initially recognized at fair value, which is considered equivalent to their cost, and subsequently accounted at lowest of cost and net realisable value. Fair value of repossessed collateral initially is determined based on valuation performed by independent certified valuation specialist. No impairment is recognised for repossessed collateral during the year. Additional description on repossessed collaterals is provided in note 35.

As at 31 December 2015 Financial assets included receivables from client amounting to 80,707 EUR from client related to insurance of collateral and real estate tax expenses. While raising provisions for impairment of related loan balance, the Bank has created provisions amounting to 100% of these receivables as well. Other financial assets are not overdue and are not impaired.

NOTE 33 ASSETS UNDER MANAGEMENT

	31.12.2015. EUR	**31.12.2014. EUR**
Legal entities:		
- residents	-	10,445,293
- non-residents	100,582,655	115,182,208
Private individuals:		
- non-residents	7,304,456	3,655,768
Total assets under management	**107,887,111**	**129,283,269**

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

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 34 AVAILABLE-FOR-SALE FINANCIAL ASSETS

Available-for-sale financial assets are comprised of VISA Europe Limited shares. Previously these shares were accounted at their nominal value of 10 EUR, as there were no indications as to the approximate amount of their fair value. Due to purchase of VISA Europe Limited shares, which was announced by VISA Inc. in 2015, the Bank has received information on probable payments, which will be made to the Bank to compensate for the value of shares held. These payments will consist of cash payment, preference shares and deferred earn-out payment. Due to high uncertainty factor attached to the valuation of preference shares and deferred earn-out payment, as well as problems with determining their potential amount under current conditions, as at 31 December 2015 the Bank has recognised only cash payment as the equivalent of the fair value of VISA Europe Limited shares.

NOTE 35 LOSS FROM SALE OF REPOSSESSED COLLATERAL

During 2015 while recovering bad loans, Bank has repossessed and recognised on the balance sheet 4 collaterals (real estate) for the total amount of 2,545,506 EUR.

During the year the Bank sold 5 real estate objects, which were previously repossessed and recognised on the balance sheet of the Bank. As a result of sale of these objects, the Bank generated net profit of 17,184 EUR.

In 2014 the Bank has repossessed from its borrowers and recognised in the balance sheet 6 collaterals available for further sale (real estate) for the total amount of 676,205 EUR.

During the year the Bank sold 4 real estate objects, which were previously recognised in the balance sheet of the Bank (one object in 2012, one in 2013 and two in 2014) for the total amount of 1,248,288 EUR. As a result of sale of these objects (i.e. from the difference arising between the balance sheet value and the selling price), the Bank in 2014 incurred losses of 1,438,130 EUR.

The biggest portion of loss (1,303,068 EUR from 1,438,130 EUR) arose on one transaction where the Bank sold real estate object recognised in the balance sheet of the Bank in 2013 located in Cerkovnaja street 19, Odesa (factory and warehouse complex with approximate space of 26,000 m^2). This object was recognised in the balance sheet of the Bank in September 2013 based on the valuation performed on 26 June 2013 and sold in September 2014 for the price, which was significantly below the valuation price and the balance sheet value. Such a significant deviation between price included into valuation made in June 2013 and selling price of September 2014 was determined by the following factors:

(1) The Bank obtained ownership rights for this object after complex and prolonged litigation, which took place in 2012 and 2013. The owner of the object (provider of the pledge) made all possible effort in preventing the Bank from exercising the mortgage rights, and understanding that his position is unsupported and there is no opportunity of keeping the ownership of the object, was not taking any care of the object until the moment when ownership rights were passed to the Bank. Although legal ownership passed to the Bank in September 2013, actual transfer of ownership occurred only at the very end of 2013.

(2) The Bank was forced to sell object in September 2014, as after the actions of the former owner described in point (1) above and after winter of 2013-2014, the preservation of the object required significant additional investments, especially in light of approaching winter of 2014-2015. Management and repairs of such specific objects is not the operating activity of the Bank, therefore, the Bank considered that realisation of the object for the maximum possible selling price of that moment is rational decision, moreover, without additional investments, the condition of the object continued to deteriorate.

(3) At the moment of sale, potential customers knew that starting from 2015 new real estate tax rate will be enacted in Ukraine, significantly increasing maintenance costs of similar objects, especially taking into account the large space occupied – approximately 26,000 m^2. This factor also significantly decreased the potential selling price of the object.

NOTES TO THE FINANCIAL STATEMENTS (continued)

35 LOSS FROM SALE OF REPOSSESSED COLLATERAL (continued)

Taking into account the considerations above, the Bank considers that these losses are fully attributable to 2014 and should be qualified not as a mistake in initial valuation of collateral, but as one-off case related to misconduct of borrower, who to the biggest extent possible was preventing the Bank from exercising its legal rights and interests, which resulted in significant damage to the pledged object. This position is substantiated by sales of other real estate objects of the Bank, where losses (as percentage from the carrying value of the object) are significantly lower and are mainly related to the currency rate fluctuations on Ukrainian national currency at the moment of transaction.

NOTE 36 RETURN ON CAPITAL AND RETURN ON ASSETS

	2015	2014
Return on capital (ROE) (%)	(4.39) %	(4.79)%
Return on assets (ROA) (%)	(0.24) %	(0.37)%

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 Bank's financial position as at 31 December 2015.

At the end of 2015, the Bank presented for approval of the FCMC the bond program prospectus, and it was registered by the FCMC Council at the very beginning of 2016. The prospectus provides that the Bank is entitled to hold public offering of bonds for 20 million US dollars. It means that the Bank can launch its first issuance of bonds. Specific parameters of the first bond issuance will be formulated in the respective bond issuance documents and will become available when the Bank starts the first drawdown.