JSC "REGIONALA INVESTICIJU BANKA"

ANNUAL REPORT
FOR THE YEAR ENDED 31 DECEMBER 2012

CONTENTS

JSC "Regionala investiciju banka"

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

Phone: (371) 67508989

Facsimile: (371) 67508988

Registration number: 4000 356 3375

Report of the Management

In 2012 JSC "Regionala investiciju banka" (hereinafter – the Bank) continued its successful development with positive growth. Following global and European bank capitalisation trends, one of the Bank's main tasks in 2012 was to fulfil increased capital requirements, which the Bank fully complied with. The Bank's customer base as well as assets and deposits increased, while its loan portfolio slightly decreased as the Bank took steps to improve its quality. The Bank's successful development and positive growth in 2012 are confirmed by its profit of LVL 1.539 million, which will be retained to increase the shareholders' equity.

Overall economic situation

In 2012 Latvia's economy continued the positive growth trend that began in previous years. It should be noted that the overall GDP growth of about 5.5% in 2012 is the best GDP growth rate across the EU. This confirms that the internal devaluation measures and the ability of the labour market to flexibly adapt to the new requirements during the crisis were able to ensure Latvia's long-term development and to improve the competitiveness of many industries. The increased competitiveness is evidenced by export growth and its increasing impact on Latvia's overall economic development rates. In addition, economic growth was achieved despite the unconvincing global growth rates and problems in the European Union, Latvia's key export market.

The year 2012 was marked as a year of stabilisation on Latvia's financial markets. After the shock suffered in 2011, when Latvijas Krājbanka was suspended and groundless rumours circulated about the financial instability of other banks, the Latvian banking sector began to regain consumer trust in 2012. 2012 was successful for the banking sector also in financial terms, with profits being reported again after a three-year break. Some other positive trends could also be seen, such as a slower decrease in bank loan portfolios and a gradual increase in deposits.

2012 also saw an increase in foreign investors' interest in Latvia, especially after repayment of the IMF loan and fulfilment of the euro zone entry criteria. This was also evidenced by the Latvian government's ability to attract resources for the second time by successfully issuing 1,250 million USD denominated 7-year bonds on foreign financial markets at a record low rate.

Unlike Latvia, Ukraine saw a sharp drop in economic growth rates in 2012. Although the first quarters of 2012 saw a GDP growth of 2% and 3% respectively, the economy rapidly cooled down in the second half of 2012, and according to preliminary estimates the total GDP growth in 2012 was a mere 0.2%, which is a considerable drop compared to the 5.2% growth in 2011. The drop in economy growth rates is mainly due to the adverse situation in the country's export markets, especially the poor economic activity growth rates in the EU, because export represents more than 50% of the country's GDP. The GDP growth rates were substantially affected also by hosting the European football championship, which gave an important contribution to growth in 2011. Ukraine's construction sector decreased by 13.8% in 2012 compared to the previous year, when much of the construction work was carried out to host the championship. Another factor adversely affecting economic activity was a 4.5% drop in agricultural production, which was due to a comparatively poorer crop than in 2011.

The previous year in Ukraine's financial sector could be called a year of turnaround because the banking sector reported profits again after a three-year break. The key banking sector trends in 2012 include an increase in bank assets, improved quality of loan portfolios, and capital growth. It should be noted, however, that the largest rating agencies were cautious about the industry's successful development in the future and even reduced the credit ratings for a number of banks operating in the region in 2012.

Bulgaria's situation in the post-crisis period may be described as a prolonged cycle of slow economic growth. While overall the economy continues to grow and has shown positive growth for ten consecutive quarters, the growth rates are poor and considerably lower than before the crisis. It should be noted, however, that the situation in the country is closely linked to the poor economic activity growth rates across the region, especially Southern Europe, where many countries are introducing measures to overcome the crisis and reduce their national debt.

The Bank's operations in the reporting year

The Bank's assets and deposits increased in the reporting period and reached record highs in its history. The Bank's assets reached LVL 340.48 million at 31 December 2012, showing a 43.6% growth compared to the end of 2011. The Bank's deposit portfolio grew by 41.8% over this period and reached LVL 304.9 million at 31 December 2012.

One of the Bank's priorities in 2012 was to improve the quality of its loan portfolio, therefore the portfolio decreased by 13.1% compared to 2011 and was LVL 72.83 million at 31 December 2012.

Report of the Management (continued)

The Bank's Council was changed in March 2012 and now has five members. The composition of the Board was also changed – starting with 8 January 2013 Olexandr Kovalsky is approved as a Deputy Chairman of the Board.

In December 2012 the latest changes were made to the Bank's ownership, and its share capital was increased by LVL 5.2 million to reach LVL 22.725 million. The Bank's largest shareholder is Pivdennyi Bank plc with ownership of 81.85%, while the remaining 18.15% is held by two legal entities and seven individuals.

Compared to the end of 2011 the Bank's customer base grew by 12%, with a pro rata (12%) increase in outgoing transfers. The number of payment cards grew by 20% compared to the relevant period in the previous year, and payment card turnover increased by 32% to reach LVL 14.02 million in 2012.

In 2012 the Bank started to issue *World Signia* payment cards to its customers, and nine customers are now using this exclusive payment card with the Bank's assistance.

Continuing the positive growth trend started in 2011, the documentary transaction volume increased by 47.79% in 2012 to reach LVL 92.3 million at 31 December 2012.

In the first six months of 2012 the Bank actively pushed the implementation of the new e-Broker service, and since July 2012 the Bank's customers trading in financial instruments on a daily basis have been able to use the e-Broker service, which allows them to close deals in company shares traded on NASDAQ OMX Riga, Tallinn and Vilnius stock exchanges without the assistance of the Bank's broker.

In September 2012 the Financial and Capital Market Commission imposed on the Bank an individual capital requirement of 17.6% (previously - 15.6%), which the Bank observes and complies with.

In terms of IT the Bank has upgraded a number of software programs and improved its IT governance processes, with one of its latest Internet bank versions featuring the Regular Payment service, which facilitates the administration of daily transfers for the Bank's customers.

To optimise the signing and sending of business correspondence, the Bank continues work on the e-Signature project, which is to be implemented by the end of 2013.

In 2012 the Bank recruited 18 new employees and its total staff count was 127 at 31 December 2012.

In 2012 the Bank started to liquidate its Bulgarian branch, and the liquidation process is under way. The Bulgarian branch is to be closed down in the spring of 2013.

Plans and prospects for the next year

In 2013 the Bank plans to continue its development, while maintaining positive growth. The Bank will continue to build its customer base, with the focus on servicing wealthy individuals and offering private banking services.

In terms of products the Bank plans to improve its Internet bank and to update the use of other means of remote account management. There are also plans to expand the functionality of the securities service and to increase the number of Repo deals in financial instruments.

In late 2011 the Bank started to develop a new service – investment in gold. The Bank's customers are now able to make investment in gold using the Bank's gold correspondent accounts, and it is also possible to buy gold bullions. In the first quarter of 2013, when implementation of the new service at the Bank is complete, there are plans to provide the storage of gold at the Bank.

In January 2013 the Bank obtained a licence from the international payment card organisation VISA Europe, which will allow the Bank to successfully continue the process of acquiring payment cards. In late 2013 the Bank's customers will be able to acquire MasterCard and Maestro as well as VISA and VISA Electron payment cards at their points of sale, including the Internet.

Haralds Abolins
Chairman of the Board, President

Iurii Rodin
Chairman of the Council

Riga, 11 March 2013

THE SUPERVISORY COUNCIL AND THE BOARD OF DIRECTORS OF THE BANK

As at 31 December 2012 and as at the date of signing the accounts:

The Council

		Date of appointment
Iurii Rodin	Chairman of the Council	Re-elected – 24.02.2012
Mark Bekker	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

Haralds Abolins	Chairman of the Board and President	Re-elected – 28.06.2012
Olexandr Kovalsky	Deputy Chairman of the Board	08.01.2013
Daiga Muravska	Member of the Board	Re-elected – 28.06.2012

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 8 to 54 are prepared in accordance with the source documents and present fairly the financial position of the Bank as at 31 December 2012 and the results of its operations and cash flows for the reporting year 2012.

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.

Haralds Abolins
Chairman of the Board, President

Iurii Rodin
Chairman of the Council

Riga, 11 March 2013

Auditors' report

Translation from Latvian original*

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of AS Reģionālā Investīciju banka

Report on the Financial Statements

We have audited the accompanying financial statements on pages 8 to 54 of AS Reģionālā Investīciju banka which comprise the statement of financial position as of 31 December 2012 and the statements of comprehensive income, changes in equity and cash flows for the year then ended and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the International Financial Reporting Standards as adopted by the European Union, and for such internal control as management determines is necessary to enable the preparation of 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 and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the 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.

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the AS Reģionālā Investīciju banka as of 31 December 2012, and of its financial performance and its cash flows for the year then ended in accordance with the International Financial Reporting Standards as adopted by the European Union.

Report on Other Legal and Regulatory Requirements

We have read the Management Report set out on pages 3 to 4 and did not identify material inconsistencies between the financial information contained in the Management Report and that contained in the financial statements for 2012.

PricewaterhouseCoopers SIA
Certified audit company
Licence No. 5

Ilandra Lejiņa
Member of the Board

Terēze Labzova
Certified auditor in charge
Certificate No. 184

Riga, Latvia
11 March 2013

* 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.

PricewaterhouseCoopers SIA, Kr. Valdemara iela 21-21, Riga LV-1010, Latvia
T: +371 6709 4400, F:+371 6783 0055, www.pwc.lv

Statement of Comprehensive Income for the year ended 31 December 2012

	Notes	2012 LVL	2011 LVL
Interest income	5	14,191,474	7,743,239
Interest expense	5	(8,793,542)	(4,546,339)
Net interest income		**5,397,932**	**3,196,900**
Provisions for loan impairment	11	(3,200,189)	(4,089,349)
Net interest income/ (expense) after provision for loan impairment		**2,197,743**	**(892,449)**
Fee and commission income	6	3,997,785	3,304,094
Fee and commission expense	6	(1,228,464)	(920,045)
Net fee and commission income	6	**2,769,321**	**2,384,049**
Profit/ (loss) on securities trading, net		120	(9,027)
Profit/ (loss) from revaluation of securities at fair value through profit and loss account		553,481	(584,739)
Profit/ (loss) on derivative financial instruments revaluation		(97,870)	80,966
Profit on operation with foreign exchange, net		762,104	537,494
Profit/ (loss) from revaluation of foreign exchange, net		65,887	(168,224)
Other operating income		589,261	122,115
Administrative expense	7	(4,204,325)	(3,691,082)
Amortisation and depreciation charge	13, 14	(225,011)	(270,312)
Other operating expense		(67,184)	(62,736)
Profit from decrease in provisions		26,475	-
Profit/ (loss) before income tax		**2,370,002**	**(2,553,945)**
Income tax expense	8	-	-
Amount of tax paid abroad	8	(816,577)	(241,755)
Deferred income tax	8	(13,577)	9,386
Net profit/ (loss) for the year		**1,539,848**	**(2,786,314)**
Total comprehensive income/ (loss) for the year attributable to the owners of the Bank		**1,539,848**	**(2,786,314)**

The financial statements on pages 8 to 54 have been approved by the Supervisory Council and the Board of Directors of the Bank and signed on their behalf by:

Haralds Abolins
Chairman of the Board, President

Iurii Rodin
Chairman of the Council

Riga, 11 March 2013

The accompanying notes on pages 12 to 54 are an integral part of these financial statements.

Statement of Financial Position as at 31 December 2012

	Notes	31.12.2012 LVL	31.12.2011 LVL
Assets			
Cash and balances with the Bank of Latvia	9	44,440,857	11,880,259
Balances due from banks	10	207,381,802	129,980,150
Loans and advances to customers	11	72,830,308	83,836,244
Financial assets at fair value through profit or loss	12	13,793,922	9,083,444
Derivative financial instruments	20	112,637	293,827
Intangible assets	13	148,716	259,546
Property and equipment	14	225,108	289,615
Other assets		1,477,816	1,016,784
Deferred expenses		68,459	71,752
Deferred income tax asset	19	-	6,628
Corporate income tax	30	-	358,892
Total assets		**340,479,625**	**237,077,141**
Liabilities			
Balances due to banks	16	1,690,733	1,180,403
Balances due to customers	15	304,888,231	215,504,303
Derivative financial instruments	20	157,219	240,539
Other financial liabilities	17	2,968,887	1,624,702
Deferred income and accrued expenses	18	661,491	513,988
Deferred income tax liability	19	6,949	-
Subordinated loan	31	4,423,721	5,470,660
Total liabilities		**314,797,231**	**224,534,595**
Equity			
Share capital	21	22,725,000	11,125,000
Retained earnings		1,417,546	4,203,860
Comprehensive income / (loss) for the year		1,539,848	(2,786,314)
Total equity		**25,682,394**	**12,542,546**
Total liabilities and equity		**340,479,625**	**237,077,141**
Commitments and contingent liabilities			
Contingent liabilities	22	6,016,694	4,991,407
Financial commitments	22	19,170,535	13,402,669

The financial statements on pages 8 to 54 have been approved by the Supervisory Council and the Board of Directors of the Bank and signed on their behalf by:

Haralds Abolins
Chairman of the Board, President

Iurii Rodin
Chairman of the Council

Riga, 11 March 2013

The accompanying notes on pages 12 to 54 are an integral part of these financial statements.

Statement of Changes in Equity for the year ended 31 December 2012

	Paid-in share capital	Retained earnings	Total
	LVL	**LVL**	**LVL**
Balance as at 31 December 2010	**10,200,000**	**4,203,860**	**14,403,860**
Increase in paid-in share capital	925,000	-	925,000
Comprehensive loss for the year	-	(2,786,314)	(2,786,314)
Balance as at 31 December 2011	**11,125,000**	**1,417,546**	**12,542,546**
Increase in paid-in share capital	11,600,000	-	11,600,000
Comprehensive income for the year	-	1,539,848	1,539,848
Balance as at 31 December 2012	**22,725,000**	**2,957,394**	**25,682,394**

The accompanying notes on pages 12 to 54 are an integral part of these financial statements.

Statement of Cash Flows for the year ended 31 December 2012

	Notes	2012 LVL	2011 LVL
Cash flows from operating activities			
Interest received		12,526,015	6,150,752
Interest paid		(9,284,024)	(5,093,091)
Fees and commission received		3,997,785	3,304,094
Fees and commission paid		(1,228,464)	(920,045)
Income / (expense) on securities trading		120	(9,027)
Income on foreign exchange		762,104	537,494
Other operating income		589,261	122,115
Personnel expenses paid		(2,482,508)	(2,327,237)
Administrative and other operating expenses		(1,789,001)	(1,426,581)
Income tax paid		(816,577)	(241,755)
Cash flows generated from operating activities before changes in operating assets and liabilities		**2,274,711**	**96,719**
Changes in operating assets and liabilities			
Net (increase)/ decrease of securities at fair value through profit and loss account		(3,968,279)	669,610
Net increase of balances due from banks		(12,430,265)	(1,635,391)
Net (increase) / decrease of loans and advances to customers		7,979,277	(24,437,854)
Net (increase) / decrease of other assets		(457,740)	202,845
Net increase of balances due to customers		96,416,340	52,730,963
Net increase in other liabilities		1,877,054	623,170
Net cash and cash equivalents generated from operating activities		**91,691,098**	**28,250,062**
Cash flows from investing activities			
Purchase of intangible assets		(15,099)	(17,691)
Purchase of fixed assets		(34,575)	(47,801)
Net cash and cash equivalents used in investing activities		**(49,674)**	**(65,492)**
Cash flows from financing activities			
Proceeds from share issue		11,600,000	925,000
Subordinated loan received		7,587,000	5,440,000
Repayments of subordinated loan		(8,191,830)	-
Net cash and cash equivalents generated from financing activities		**10,995,170**	**6,365,000**
Effect of exchange rates on cash and cash equivalents		(5,099,974)	1,739,487
Net increase in cash and cash equivalents		**97,536,620**	**36,289,057**
Cash and cash equivalents at the beginning of the year	**23**	129,500,953	93,211,896
Cash and cash equivalents at the end of the year	**23**	**227,037,573**	**129,500,953**

The accompanying notes on pages 12 to 54 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. In October 2009 opened its first branch in Bulgarian town Varna. 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 11 March 2013.

NOTE 2 OPERATING ENVIRONMENT OF THE BANK

Instability in the global and Latvian financial markets and economies
As it was seen in 2012, the global economic recovery after the crisis experienced in 2008-2009 is protracted and there is a quite high probability that in some of the developed economies economic stagnation will continue also in 2013 or even lapse into a deep recession.

Currently, the greatest concern is about the Eurozone member states which showed a negative GDP growth – 0.6% during the fourth quarter of 2012. Despite the facts that for some time Central governments have overcome the debt crisis in Europe, that for Southern European governments attraction of necessary funding became easier and at lower rates, still there is no clear vision as to how to ensure economic recovery, creation of new job positions and healthy GDP growth.

Taking into account abovementioned facts, situation in the financial sector could be described as unstable. Currently, financial institutions have recovered after the liquidity crisis experienced in 2009, however this market segment has not yet presented a healthy profit and asset growth.

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 recurrence of the global economy downturn, the actual realizable value on foreclosure may differ from the value ascribed in estimating allowances for impairment.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the significant accounting policies, all of which have been applied consistently throughout the years 2011 and 2012, are set out below:

(a) Reporting currency

The tabular amounts in the accompanying financial statements are reported in Latvian lats (LVL), unless otherwise stated.

(b) Basis of preparation

These financial statements are prepared in accordance with International Financial Reporting Standards (hereinafter - IFRS) as adopted in the European Union, 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 and derivative financial instruments.

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

The accounting policies used in the preparation of the financial statements for the year ended 31 December 2012 are consistent with those used in the annual financial statements for the year ended 31 December 2011, 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. Interest income includes coupons earned on trading securities.

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. Other fees and commissions, including those related to trust activities, are credited and/or charged to the statement of comprehensive income as earned / incurred.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(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 'Latvian lats' ('LVL'), which is the Bank's functional and presentation currency.

Transactions and balances
Transactions denominated in foreign currencies are recorded in lats at rates of exchange set forth by the Bank of Latvia at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into lats at the rate of exchange prevailing at the end of the period. Any gain or loss resulting from a change in rates of exchange subsequent to the date of the transaction is included in the statement of comprehensive income as a profit or loss from revaluation of foreign currency positions.

The principal rates of exchange (LVL to 1 foreign currency unit) set forth by the Bank of Latvia and used in the preparation of the Bank's balance sheets were as follows:

Reporting date	USD	EUR	BGN	UAH
As at 31 December 2012	0.531	0.702804	0.359	0.0660
As at 31 December 2011	0.544	0.702804	0.359	0.0677

(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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(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.

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

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

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(h) Credit related commitments
The Bank enters into credit related commitments, including 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.

(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 statement of comprehensive income. 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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(m) Fair values of financial assets and liabilities
Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. 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.

(n) 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.

(o) 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.

(p) 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.

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:

Office equipment	10 years
Computers	3 years
Transport	5 years

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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(q) 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.

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

(s) 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.

(t) 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 or insurance arrangements where appropriate, and the amounts and timings of such outflows and recoveries, if any.

(u) 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.

(v) 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 76.2% (2011: 72.84%) 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.

(w) 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.

(x) 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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(y) Debt securities in issue

Debt securities in issue include bonds issued by the Bank. Debt securities are stated at amortised cost. If the Bank purchases its own debt securities in issue, they are removed from the balance sheet and the difference between the carrying amount of the liability and the consideration paid is included in gains arising from retirement of debt.

(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 LVL 103.2 thousand.

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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(bb) Adoption of new or revised standards and interpretations

The following new and amended IFRSs and interpretations became effective in 2012, but are not relevant for the Bank's operations and did not have an impact on these financial statements.

Amendments to IFRS 7 "Financial instruments: Disclosures" on transfers of assets (effective for annual periods beginning on or after 1 July 2011).

Amendments to IFRS 1 "First time adoption" on fixed dates and hyperinflation (effective for annual periods beginning on or after 1 July 2011).

Amendments to IAS 12 "Income taxes" on deferred tax (effective for annual periods beginning on or after 1 January 2012).

Certain new standards and interpretations have been published that become effective for the accounting periods beginning on or after 1 January 2013 or later periods and which are not relevant to the Bank or are not yet endorsed by the EU.

Amendments to IAS 19 "Employee benefits" (effective for annual periods beginning on or after 1 January 2013).

Amendments to IAS 1 "Financial statement presentation" regarding other comprehensive income (effective for annual periods beginning on or after 1 January 2012, endorsed by the EU on June 2012).

IFRS 9 "Financial Instruments Part 1: Classification and Measurement" (effective for annual periods beginning on or after 1 January 2015; not yet endorsed by the EU).

IFRS 10 "Consolidated financial statements" (effective for annual periods beginning on or after 1 January 2013, endorsed by the EU in December 2012 for annual periods starting on or after 1 January 2014).

IFRS 11 "Joint arrangements" (effective for annual periods beginning on or after 1 January 2013, endorsed by the EU in December 2012 for annual periods starting on or after 1 January 2014).

IFRS 12 "Disclosures of interests in other entities" (effective for annual periods beginning on or after 1 January 2013, endorsed by the EU in December 2012 for annual periods starting on or after 1 January 2014).

Amendments to IFRS 10, 11 and 12 on transition guidance (effective for annual periods beginning on or after 1 January 2013, endorsed by the EU in December 2012 for annual periods starting on or after 1 January 2013).

IFRS 13 "Fair value measurement" (effective for annual periods beginning on or after 1 January 2013, endorsed by the EU in December 2012).

IAS 27 (revised 2011) "Separate financial statements" (effective for annual periods beginning on or after 1 January 2013, endorsed by the EU in December 2012 for annual periods starting on or after 1 January 2014).

IAS 28 (revised 2011) "Associates and joint ventures" (effective for annual periods beginning on or after 1 January 2013, endorsed by the EU in December 2012 for annual periods starting on or after 1 January 2014).

Amendments to IFRS 7 "Financial instruments: Disclosures" on offsetting financial assets and financial liabilities (effective for annual periods beginning on or after 1 January 2013, endorsed by the EU on December 2012).

Amendments to IAS 32 "Financial instruments: Presentation" on offsetting financial assets and financial liabilities (effective for annual periods beginning on or after 1 January 2014, endorsed by the EU on December 2012).

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 IFRS 1 "First time adoption" on government loans (effective for annual periods beginning on or after 1 January 2013, not yet endorsed by the EU).

Improvements to IFRS (issued in May 2012; most of the amendments are effective for annual periods beginning on or after 1 January 2013, not yet endorsed by the EU):

- IFRS 1 "First time adoption";
- IAS 1 "Financial statement presentation";
- IAS 16 "Property, plant and equipment";
- IAS 32 "Financial instruments: Presentation";
- IAS 34 "Interim financial reporting".

Amendments to IFRS 10, IFRS 12 and IAS 27 on investment entities (effective for annual periods beginning on or after 1 January 2014, not yet endorsed by the EU).

IFRIC 20, "Stripping costs in the production phase of a surface mine" (effective for annual periods beginning on or after 1 January 2013, endorsed by the EU on December 2012).

NOTES TO THE FINANCIAL STATEMENTS (continued)

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.

The main unit responsible for determination, evaluation and oversight of the risks is the Risk Management Department, which is an independent unit whose functions are separated from the functions of the business units.

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

(a) Credit risk

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

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

The Bank divides up and oversees its credit risk by setting limits of various types and categories: acceptable risk limits for each borrower, group of related borrowers, geographical regions, business sectors, type and value of collateral, currency, term and ratings granted by international agencies. Credit risk exposures are monitored on a revolving basis through regular assessments of borrowers’ ability to meet interest and principal 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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4 FINANCIAL RISK MANAGEMENT (continued)

(a) Credit risk (continued)

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

	31.12.2012 LVL	31.12.2011 LVL
Credit risk exposures relating to on-balance sheet assets are as follows:		
Due from credit institutions	207,381,802	129,980,150
Loans to customers	72,830,308	83,836,244
Financial assets at fair value through profit or loss	13,793,922	9,083,444
Other assets	1,477,816	1,016,784
Total	**295,483,848**	**223,916,622**
Credit risk exposures relating to off-balance sheet items are as follows:		
Contingent liabilities	6,016,694	4,991,407
Financial commitments	19,170,535	13,402,669
Total	**25,187,229**	**18,394,076**

(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 has exposure to the effects of fluctuations in prevailing foreign currency exchange rates as a result of its financial position and cash flows. The Bank seeks to match assets and liabilities denominated in foreign currencies in order to avoid foreign currency exposures. The Board has set limits on the level of exposure by currency, which is monitored on a daily basis. 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 2012 the Bank was in compliance with those limits (see Note 25).

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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4 FINANCIAL RISK MANAGEMENT (continued)

(c) Currency risk (continued)

Sensitivity Analysis
The following table shows the sensitivity of profit/loss and equity to currency exchange rate fluctuations at the end of the reporting period, with other conditions constant:

31.12.2012	Effect on equity		Effect on profit/loss		31.12.2011	Effect on equity		Effect on profit/loss	
	+100 bps	-100 bps	+100 bps	-100 bps		+100 bps	-100 bps	+100 bps	-100 bps
USD	233	233	-12	12	**USD**	-138	138	40	-40
EUR	-9	9	16	-16	**EUR**	-35	35	9	-9
LVL	201	-201	1	-1	**LVL**	70	-70	1	-1
Other	-	-	-	-	**Other**	-	-	-	-
Total	**-41**	**41**	**5**	**-5**	**Total**	**-103**	**103**	**50**	**-50**

The following table shows the average annual sensitivity of profit/loss and equity to currency exchange rate fluctuations during the reporting period, with other conditions constant:

31.12.2012	Effect on equity		Effect on profit/loss		31.12.2011	Effect on equity		Effect on profit/loss	
	+100 bps	-100 bps	+100 bps	-100 bps		+100 bps	-100 bps	+100 bps	-100 bps
Total	**-164**	**164**	**17**	**-17**	**Total**	**-111**	**111**	**31**	**-31**

(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).

In order to evaluate interest rate risk, evaluation is made of the impact of interest rate changes on the Bank's economic value, including evaluation of interest rate risk from the revenue perspective and the economic value perspective. In addition, interest rate risk stress testing is performed.

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.

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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4 FINANCIAL RISK MANAGEMENT (continued)

(d) Interest rate risk (continued)

The following table shows the sensitivity of profit/loss and equity to interest rate fluctuations with other conditions constant:

31.12.2012	Effect on equity		Effect on profit/loss		31.12.2011	Effect on equity		Effect on profit/loss	
	+100 bps	-100 bps	+100 bps	-100 bps		+100 bps	-100 bps	+100 bps	-100 bps
USD	-141	141	1 404	- 1 404	**USD**	-121	121	1 080	-1 080
EUR	-133	133	21	-21	**EUR**	-190	190	195	-195
LVL	-166	166	93	-93	**LVL**	-100	100	-8	8
Other	-	-	24	-24	**Other**	-	-	4	-4
Total	**-441**	**441**	**1 542**	**-1 542**	**Total**	**-411**	**411**	**1 271**	**-1 271**

The following table shows the average annual sensitivity of profit/loss and equity to interest rate fluctuations, with other conditions constant:

31.12.2012	Effect on equity		Effect on profit/loss		31.12.2011	Effect on equity		Effect on profit/loss	
	+100 bps	-100 bps	+100 bps	-100 bps		+100 bps	-100 bps	+100 bps	-100 bps
Total	**-403**	**403**	**1 460**	**-1 460**	**Total**	**-447**	**447**	**1 017**	**-1 017**

(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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4 FINANCIAL RISK MANAGEMENT (continued)

(e) Liquidity risk (continued)
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 30% of the Bank's current liabilities.

(f) Capital adequacy
Capital adequacy refers to the sufficiency of the Bank's capital resources to cover risks resulting from the Bank's operating activities.

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

The Bank also evaluates whether compliance with the minimal capital requirements ensures that the capital of the Bank is sufficient to cover all possible losses associated with all of the above mentioned risks.

Moreover, the Bank has developed internal documentation and regulations according to which it determines the amount of necessary capital for substantial risks to which minimal capital requirements are not set (e.g., interest rates risk, liquidity risk, country risk, and other substantial risks).

Calculated in accordance with the FCMC requirements, the Bank's capital adequacy ratio as at 31 December 2012 was 22.13% (as at 31 December 2011 14.50%), which is above the minimum required by the FCMC since year 2007. FCMC requires Latvian banks to maintain a capital adequacy ratio of 8% of weighted assets and off-balance sheet items which are calculated in accordance with the rules set by FCMC (see also Note 24). According to the requirements of FCMC individual capital requirement was set for the Bank for 2012 at 15.6%, which was ensured by the Bank until the term agreed with FCMC – 30.04.2012. In September 2012 the FCMC has set individual capital requirement for the Bank at 17.6% which the Bank observes and complies with.

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

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

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 4 FINANCIAL RISK MANAGEMENT (continued)

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

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

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

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

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

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

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

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

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

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 5 INTEREST INCOME AND EXPENSE

	2012 LVL	2011 LVL
Interest income		
Loans and advances to legal entities	5,544,157	4,824,384
Loans and advances to private individuals	220,373	265,549
Balances due from banks	7,867,724	1,995,845
Trading securities	559,220	657,461
Total interest income	**14,191,474**	**7,743,239**
Interest expense		
Due to private individuals	(1,009,416)	(945,490)
Due to legal entities	(6,369,898)	(3,142,629)
Balances due to banks	-	(1,471)
Subordinated loan	(472,652)	(61,216)
Other liabilities	(941,576)	(395,533)
Total interest expense	**(8,793,542)**	**(4,546,339)**
Net interest income	**5,397,932**	**3,196,900**

NOTE 6 FEE AND COMMISSION INCOME AND EXPENSE

	2012 LVL	2011 LVL
Fee and commission income		
Money transfers	2,758,535	2,388,206
Loan related fees	611	2,918
Accounts servicing	315,908	247,830
Letters of credit	320,928	212,453
Sale of deposit certificates	-	240
Commission income on transactions with financial instruments	34,034	75,798
Commission income on current accounts	15,563	18,764
Income from general services	56,024	43,236
Other commissions (DIGIPAS)	23,737	13,680
Interbank commission income	73,759	52,668
Commission for dealing with cards	104,242	79,665
Income from currency exchange	179,678	69,435
Other income	114,766	99,201
Total fee and commission income	**3,997,785**	**3,304,094**
Fee and commission expense		
Money transfers	(1,178,500)	(650,512)
Other expense	(49,964)	(269,533)
Total fee and commission expense	**(1,228,464)**	**(920,045)**
Net fee and commission income	**2,769,321**	**2,384,049**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 7 ADMINISTRATIVE EXPENSE

	2012 LVL	2011 LVL
Remuneration paid to personnel	1,790,469	1,652,188
Rent expense	306,226	291,896
Office and equipment maintenance	75,590	71,653
Remuneration paid to the members of the Council and the Board	221,373	234,293
Security services	15,292	41,488
Public utilities	36,703	35,297
State compulsory social insurance contributions	469,935	440,442
Communication expense	214,919	221,234
Consulting and professional fees	463,115	199,293
Set-up and maintenance costs of information systems	77,250	57,485
Business trips	76,730	88,953
Transportation	41,563	36,926
Health insurance	18,765	15,946
Advertising and marketing	2,010	2,017
Penalties	208	10,092
Other administrative expense	394,177	291,879
	4,204,325	**3,691,082**

The average number of staff employed by the Bank in 2012 was 127 (2011: 115).

NOTE 8 INCOME TAX EXPENSE

Corporate income tax for the reporting year	-	-
Amount of tax paid abroad	816,577	241,755
Change in deferred tax (see Note 19)	13,577	(9,386)
Total corporate income tax	**830,154**	**232,369**

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

Profit/ (loss) before income tax	**2,370,002**	**(2,553,945)**
Theoretically calculated tax at a tax rate of 15%	355,500	(383,092)
Profit/ (loss) from revaluation of securities at fair value through profit and loss account, net	(97,750)	89,580
Other expenses not deductible for tax purposes, net	(244,173)	284,126
Amount of tax paid abroad	816,577	241,755
Corporate income tax expense	**830,154**	**232,369**

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

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 9 CASH AND BALANCES WITH THE BANK OF LATVIA

	31.12.2012 LVL	31.12.2011 LVL
Cash	687,627	1,545,714
Balances on demand with the Bank of Latvia	43,753,230	10,334,545
	44,440,857	**11,880,259**

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 mandatory reserve maintained in accordance with the Bank of Latvia regulations. These regulations specify the minimum level of the average balance to be maintained on the Bank's correspondent account with the Bank of Latvia during each month, whilst allowing funds in the account to be used in an unrestricted manner on individual days. The minimum level of the average balance to be maintained on the Bank's correspondent account with the Bank of Latvia during the period from 24/12/2012 till 23/01/2013 has been set in amount of 12,422,741 LVL.

The Bank was in compliance with the reserve requirement of the Bank of Latvia during the reporting period.

NOTE 10 BALANCES DUE FROM BANKS

	31.12.2012 LVL	31.12.2011 LVL
Due from Republic of Latvia credit institutions	8,490,321	12,662,630
Due from non-OECD credit institutions	145,223,130	45,874,599
Due from OECD credit institutions	53,668,351	71,442,921
	207,381,802	**129,980,150**

The following table discloses balances due from banks between demand and term deposits:

On demand	180,118,610	93,536,781
Balances with maturity of three months or less	4,168,839	25,264,316
Other balances due from banks	23,094,353	11,179,053
	207,381,802	**129,980,150**

The following table discloses balances due from banks according to their ratings as at 31 December 2012 and 31 December 2011:

	31.12.2012		**31.12.2011**	
Rating	**Due from banks LVL**	**%**	**Due from banks LVL**	**%**
From Aaa to Aa3	58	0.00%	33,157,185	25.51%
From A1 to A3	52,523,410	25.33%	37,788,132	29.07%
From Baa1 to Baa3	5,508,003	2.65%	233,002	0.18%
From Ba1 to Ba3	475,230	0.23%	790,718	0.61%
From B1 to B3	11,327,240	5.46%	41,001,066	31.54%
Below B3	114,911,275	55.41%	-	-
	184,745,216	**89.08**%	**112,970,103**	**86.91%**
Without rating	22,636,586	10.92%	17,010,047	13.09%
	207,381,802	**100.00%**	**129,980,150**	**100.00%**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11 LOANS AND ADVANCES TO CUSTOMERS

(a) Analysis of loans by client type and by products

	31.12.2012 LVL	31.12.2011 LVL
Loans to legal entities	77,091,807	87,864,729
Loans to private individuals, except for mortgages	1,490,031	2,339,560
Loans to private individuals – private enterprises	-	39,872
Mortgages	2,268,765	2,873,873
Sale and repurchase agreements (reverse repo)	2,291,143	-
Less: provisions for loan impairment	(10,311,438)	(9,281,790)
Total loans and advances to customers	**72,830,308**	**83,836,244**

The following table discloses changes in provisions for loan impairment during 2012:

	Loans to legal entities	Loans to private individuals, except for mortgages	Mortgages	Total
Provisions for loan impairment as at 1 January 2012	**8,600,593**	**330,762**	**350,435**	**9,281,790**
Increase in provisions for loan impairment for the year	2,970,282	229,907	-	3,200,189
Change in provision due to loans write-offs	(1,915,473)	-	(149,264)	(2,064,737)
Impact of foreign currency revaluation	(105,818)	(7,420)	7434	(105,804)
Provisions for loan impairment as at 31 December 2012	**9,549,584**	**553,249**	**208,605**	**10,311,438**

The following table discloses changes in provisions for loan impairment during 2011:

	Loans to legal entities	Loans to private individuals, except for mortgages	Mortgages	Total
Provisions for loan impairment as at 1 January 2011	**4,724,489**	**220,287**	**77,646**	**5,022,422**
Increase in provisions for loan impairment for the year	3,706,085	110,475	272,789	4,089,349
Impact of foreign currency revaluation	170,019	-	-	170,019
Provisions for loan impairment as at 31 December 2011	**8,600,593**	**330,762**	**350,435**	**9,281,790**

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

	2012		2011	
	LVL	%	LVL	%
Trade and commercial activities	32,249,466	38.79	40,198,822	43.17
Private individuals	3,758,796	4.52	5,213,433	5.60
Agriculture and food industry	5,011,642	6.03	4,800,559	5.16
Construction and operations with real estate	16,569,359	19.93	18,457,822	19.82
Transport and communication	11,808,650	14.20	6,859,560	7.37
Industry	3,953,200	4.75	3,910,509	4.20
Tourism and hotel services, restaurant business	1,912,167	2.30	3,717,004	3.99
Financial services	4,240,886	5.10	6,112,989	6.56
Other	3,637,580	4.38	3,847,335	4.13
Loans and advances to customers (before provisions for impairment)	**83,141,746**	**100.00%**	**93,118,033**	**100.00**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11 LOANS AND ADVANCES TO CUSTOMERS (continued)

As at 31 December 2012, the total amount of loans issued to 10 largest customers was LVL 29,283,581 (2011: LVL 30,486,320), which comprises 35.22% of the total credit portfolio (2011: 32.74%). As at 31 December 2012, there were loans and advances to customers secured by deposits LVL 5,210,554.

The following table shows the information about collateral as at 31 December 2012:

	Loans to legal entities	**Loans to private individuals, except for mortgages**	**Loans to private individuals – private enterprises**	**Mortgages**	**Total**
Unsecured	3,547,089	168,089	-	209,587	3,924,765
Collateralised by:					
- residential real estate	3,521,115	-	-	827,043	4,348,158
- other real estate	44,010,931	1,321,793	-	1,232,135	46,564,859
- tradable securities	3,345,478	-	-	-	3,345,478
- cash deposits	6,480,920	149	-	-	6,481,069
- other assets	18,477,417	-	-	-	18,477,417
Total loans and advances to customers (before provisions for impairment)	**79,382,950**	**1,490,031**	**-**	**2,268,765**	**83,141,746**

The following table shows the information about collateral as at 31 December 2011:

	Loans to legal entities	**Loans to private individuals, except for mortgages**	**Loans to private individuals – private enterprises**	**Mortgages**	**Total**
Unsecured	1,566,126	171,385	-	211,335	1,948,846
Collateralised by:					
- residential real estate	4,297,095	240,533	-	691,888	5,229,516
- other real estate	42,310,765	1,366,381	-	1,900,370	45,577,516
- tradable securities	3,164,863	-	39,872	-	3,204,735
- cash deposits	8,071,355	561,261	-	70,280	8,702,896
- other assets	28,454,524	-	-	-	28,454,524
Total loans and advances to customers (before provisions for impairment)	**87,864,728**	**2,339,560**	**39,872**	**2,873,873**	**93,118,033**

Bank analyses credits and advances also based on the size of the borrower – legal person:

Big size entities – if borrower is not medium size, small size or micro entity.
Medium size entities – if borrower is an entity with annual average number of employees below 250 and turnover less than 50 million EUR in lat equivalent and/ or total assets are not in excess of 43 million EUR in lat equivalent.
Small size entities – if borrower is an entity with annual average number of employees below 50 and turnover and/ or total assets are not in excess of 10 million EUR in lat equivalent.
Micro entities – if borrower is an entity with annual average number of employees below 10 and turnover and/ or total assets are not in excess of 2 million EUR in lat equivalent.

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 2012 by credit quality:

	Loans to legal entities	Loans to private individuals, except for mortgages	Loans to private individuals – private enterprises	Mortgages	Total
Neither past due nor impaired					
- Loans to big size entities	4,569,597	-	-	-	**4,569,597**
- Loans to medium size entities	4,162,127	-	-	-	**4,162,127**
- Loans to small size entities	46,817,392	-	-	-	**46,817,392**
- Loans to private individuals	-	136,907	-	828,351	**965,258**
Total neither past due nor impaired	**55,549,116**	**136,907**	**-**	**828,351**	**56,514,374**
Past due but not impaired					
- past due 30 days	53,391	-	-	-	**53,391**
- past due from 30 to 90 days	5,510,074	-	-	-	**5,510,074**
- past due from 91 to 180 days	523,526	2,796	-	-	**526,322**
- past due from 181 to 360 days	62,367	-	-	308,532	**370,899**
- past due over 360 days	-	-	-	895,203	**895,203**
Total past due, but not impaired	**6,149,358**	**2,796**	**-**	**1,203,735**	**7,355,889**
Individually impaired loans (total amount)					
- not past due	6,088,803	12,424	-	-	**6,101,227**
- past due up to 30 days	-	16,115	-	-	**16,115**
- past due 30 – 90 days	-	-	-	-	**-**
- past due 91 – 180 days	2	-	-	-	**2**
- past due 181 – 360 days	3,427,722	3,622	-	103,909	**3,535,253**
- past due over 360 days	8,167,949	1,318,167	-	132,770	**9,618,886**
Total individually impaired loans (total amount)	**17,684,476**	**1,350,328**	**-**	**236,679**	**19,271,483**
Less: provisions for loan impairment	**(9,549,584)**	**(553,249)**	**-**	**(208,605)**	**(10,311,438)**
Net loans and advances to customers	**69,833,366**	**936,782**	**-**	**2,060,160**	**72,830,308**

Loans past due, but not impaired include all amounts due from borrowers. Amount actually overdue as at 31 December 2012 were 4,257,575 LVL.

Loans past due and individually impaired include all amounts due from borrowers. Amount actually overdue as at 31 December 2012 was 12,357,778 LVL.

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 2011 by credit quality:

	Loans to legal entities	**Loans to private individuals, except for mortgages**	**Loans to private individuals – private enterprises**	**Mortgages**	**Total**
Neither past due nor impaired					
- Loans to big size entities	4,005,574	-	-	-	**4,005,574**
- Loans to medium size entities	4,967,761	-	-	-	**4,967,761**
- Loans to small size entities	54,199,718	-	-	-	**54,199,718**
- Loans to private individuals	-	748,279	39,872	873,946	**1,662,097**
Total neither past due nor impaired	**63,173,053**	**748,279**	**39,872**	**873,946**	**64,835,150**
Past due but not impaired					
- past due up to 30 days	5,209,337	10,146	-	232,115	5,451,598
- past due 30 days to 90 days	1,234,075	4,169	-	921,143	2,159,387
- past due over 360 days	236	-	-	-	236
Total past due, but not impaired	**6,443,648**	**14,315**	**-**	**1,153,258**	**7,611,221**
Individually impaired loans (total amount)					
- not past due	6,608,916	18,258	-	6,603	6,633,777
- past due up to 30 days	133,432	-	-	-	133,432
- past due 30 – 90 days	180,243	890,721	-	-	1,070,964
- past due 91 – 180 days	1,104,682	-	-	707,297	1,811,979
- past due 181 – 360 days	3,807,436	632,622	-	-	4,440,058
- past due over 360 days	6,413,318	35,365	-	132,770	6,581,453
Total individually impaired loans (total amount)	**18,248,027**	**1,576,966**	**-**	**846,670**	**20,671,663**
Less: provisions for loan impairment	**(8,600,593)**	**(330,762)**	**-**	**(350,435)**	**(9,281,790)**
Net loans and advances to customers	**79,264,135**	**2,008,798**	**39,872**	**2,523,439**	**83,836,244**

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.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11 LOANS AND ADVANCES TO CUSTOMERS (continued)

The fair 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 2012 was as follows:

	Loans to legal entities	**Loans to private individuals, except for mortgages**	**Mortgages**
Fair value of collateral – loans past due but not impaired			
- other real estate	5,283,734	-	2,481,388
- due to customers	-	-	-
- other assets	7,098,977	-	-
Fair value of collateral – individually impaired loans			
- residential real estate	2,663,375	-	-
- other real estate	15,634,361	1,809,900	28,400
- due to customers	26,550	-	-
- other assets	5,450,407	1,022,211	-
Total	**36,157,404**	**2,832,111**	**2,509,788**

The fair 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 2011 was as follows:

	Loans to legal entities	**Loans to private individuals, except for mortgages**	**Mortgages**
Fair value of collateral – loans past due but not impaired			
- other real estate	7,343,962	69,000	1,912,528
- due to customers	2,652,299	-	-
- other assets	4,213,745	-	-
Fair value of collateral – individually impaired loans			
- residential real estate	3,268,091	638,849	-
- other real estate	16,716,707	1,803,000	565,054
- due to customers	409,088	-	70,280
- other assets	10,678,993	320,100	-
Total	**45,282,885**	**2,830,949**	**2,547,862**

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. The balance sheet value of each category of loans and advances to clients approximates its fair value as at 31 December 2011 and 2012.

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 impact of collateral at 31 December 2012:

	Assets with collateral value exceeding the loan balance		**Assets with insufficient collateral**	
	Book value of asset (before provisions for impairment)	**Fair value of collateral**	**Book value of asset (before provisions for impairment)**	**Fair value of collateral**
	LVL	**LVL**	**LVL**	**LVL**
Loans to legal entities	69,249,057	142,873,992	7,842,750	4,284,809
Loans to individuals – consumer loans	1,314,935	3,081,211	175,096	7,006
Mortgage loans	1,863,895	4,128,361	404,870	195,284
Sale and repurchase agreements (reverse repo)	2,291,143	2,408,945	-	-
Total	**74,719,030**	**152,492,509**	**8,422,716**	**4,487,099**

The impact of collateral at 31 December 2011:

	Assets with collateral value exceeding the loan balance		**Assets with insufficient collateral**	
	Book value of asset (before provisions for impairment)	**Fair value of collateral**	**Book value of asset (before provisions for impairment)**	**Fair value of collateral**
	LVL	**LVL**	**LVL**	**LVL**
Loans to legal entities	84,713,097	188,699,630	3,151,632	1,585,505
Loans to individuals, excluding mortgage loans	2,168,175	3,619,647	171,385	-
Loans to individuals - private enterprises	39,872	111,864		
Mortgage loans	2,027,203	4,954,493	846,669	635,335
Total	**88,948,347**	**197,385,634**	**4,169,686**	**2,220,840**

During 2012 loan amounting to 2,124,634 LVL was sold through cession. Claim rights were ceded for 532,000 LVL creating a loss of 1,592,634 LVL to the Bank.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 12 FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT AND LOSS

	31.12.2012 LVL	31.12.2011 LVL
Latvian government securities	11,120,491	6,546,415
Non-OECD state government debt securities	2,312,350	-
Non-OECD region corporate debt securities	355,507	2,531,386
Unquoted securities	4,748	4,864
Quoted securities	826	779
	13,793,922	**9,083,444**

Analysis of securities by category as at 31 December 2012 and 31 December 2011 is presented below:

Category 1 – includes securities with directly available market prices (regulated market) and having high liquidity allowing for quick sale for the balance sheet value.
Category 2 – includes securities which are publicly traded but having no quoting prices for at least one year or no transactions made. Fair value of these securities is calculated applying comparative methods.
Category 3 – securities which do not classify as either Category 1 or Category 2. For these securities fair value is calculated used various analytical methods which are based on analysis of similar securities and interpolation of their prices, as well as other factors.

	31.12.2012 LVL	31.12.2011 LVL
Category 1	13,793,922	9,083,444
	13,793,922	**9,083,444**

Financial assets at fair value through profit or loss are accounted at fair value that also reflects impairment loss related to credit risk. As the financial assets are accounted at fair value based on the market prices, the Bank does not analyse and follow any impairment indicators.

The following table discloses debt securities by issuers' ratings as at 31 December 2012 and 31 December 2011:

	31.12.2012		31.12.2011	
Rating	**Securities**		**Securities**	
	LVL	**%**	**LVL**	**%**
From A1 to A3	-	0.00%	-	0.00%
From Baa1 to Baa3	11,120,491	80.62%	-	0.00%
From Ba1 to Ba3	-	0.00%	6,546,415	72.07%
From B1 to B3	2,324,374	16.85%	2,194,159	24.16%
Under B3	306,588	2.22%	324,758	3.58%
	13,751,453	99.69%	**9,065,332**	**99.81%**
Without rating	42,469	0.31%	18,112	0.19%
	13,793,922	**100%**	**9,083,444**	**100%**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 13 INTANGIBLE ASSETS

The following changes in the Bank’s intangible assets took place during 2012 and 2011.

	Software 2012 LVL	Software 2011 LVL
Cost		
As at the beginning of the year	**850,920**	**833,229**
Additions	15,099	38,854
Reclassified to equipment	-	(21,163)
As at end of the year	**866,019**	**850,920**
Amortisation		
Accumulated amortisation at the beginning of the year	**591,374**	**450,342**
Charge for the year	125,929	141,032
Accumulated amortisation at the end of the year	**717,303**	**591,374**
Net book value at the beginning of the year	**259,546**	**382,887**
Net book value at the end of the year	**148,716**	**259,546**

NOTE 14 PROPERTY AND EQUIPMENT

The following changes in the Bank’s property and equipment took place during the year ended 31 December 2012:

	Transport LVL	Computers LVL	Office equipment LVL	Leasehold improvements LVL	Total LVL
Cost					
31.12.2011	**16,750**	**485,888**	**401,095**	**70,932**	**974,665**
Disposals	-	(13,851)	(1,881)	-	(15,732)
Additions	-	25,003	9,692	-	34,695
31.12.2012		**497,040**	**408,906**	**70,932**	**993,628**
Depreciation					
31.12.2011	**15,354**	**422,917**	**233,882**	**12,897**	**685,050**
On disposals	-	(13,731)	(1,881)	-	(15,612)
Charge for 2012	1,396	36,598	56,789	4,299	99,082
31.12.2012	**16,750**	**445,784**	**288,790**	**17,196**	**768,520**
Net book value 31.12.2011	**1,396**	**62,971**	**167,213**	**58,035**	**289,615**
Net book value 31.12.2012	**-**	**51,256**	**120,116**	**53,736**	**225,108**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 14 PROPERTY AND EQUIPMENT (continued)

The following changes in the Bank’s property and equipment took place during the year ended 31 December 2011:

	Transport	Computers	Office equipment	Leasehold improvements	Total
	LVL	LVL	LVL	LVL	LVL
Cost					
31.12.2010	**16,750**	**456,390**	**397,298**	**70,932**	**941,370**
Disposals	-	(14,341)	(165)	-	(14,506)
Reclassified from intangible assets	-	21,163	-	-	21,163
Additions	-	22,676	3,962	-	26,638
31.12.2011	**16,750**	**485,888**	**401,095**	**70,932**	**974,665**
Depreciation					
31.12.2010	**12,004**	**374,680**	**174,994**	**8,598**	**570,276**
On disposals	-	(14,341)	(165)	-	(14,506)
Charge for 2011	3,350	62,578	59,053	4,299	129,280
31.12.2011	**15,354**	**422,917**	**233,882**	**12,897**	**685,050**
Net book value 31.12.2010	**4,746**	**81,710**	**222,304**	**62,334**	**371,094**
Net book value 31.12.2011	**1,396**	**62,971**	**167,213**	**58,035**	**289,615**

NOTE 15 DUE TO CUSTOMERS

(a) Analysis of groups by customers

	31.12.2012	31.12.2011
	LVL	LVL
Legal entities		
- current/ settlement accounts	259,628,920	169,674,255
- term deposits	13,532,642	18,958,655
Private individuals		
- current/ settlement accounts	6,896,214	7,204,876
- term deposits	24,830,455	19,666,517
Total customer accounts:	**304,888,231**	**215,504,303**
Sector profile:		
Private companies	271,834,977	184,545,862
Private individuals	31,726,669	26,871,393
Financial institutions	1,224,784	3,973,085
Non-profit institutions	98,522	97,136
Central government	3,279	16,827
Total customer accounts:	**304,888,231**	**215,504,303**

(b) Analysis by place of residence

Residents	24,864,343	20,725,059
Non-residents	280,023,888	194,779,244
Total customer accounts:	**304,888,231**	**215,504,303**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 15 DUE TO CUSTOMERS (continued)

During the year ended 31 December 2012 average interest rate on term deposits due to customers was 4.20% (2011: 4.67%) and average interest rate on demand deposits was 0.73% (2011: from 0.07% to 1.61%). All deposits have fixed interest rates.

Economic sector concentration within customer accounts is as follows:

	2012		2011	
	LVL	**%**	**LVL**	**%**
Manufacturing	16,201,229	5.31	10,224,981	4.74
Building and real estate	14,029,662	4.60	7,476,243	3.47
Trade and commercial activities	123,090,266	40.37	90,629,730	42.05
Financial and insurance services	61,034,823	20.02	30,216,472	14.02
Transport and communications	35,880,644	11.77	42,308,122	19.63
Agriculture and food industries	2,067,015	0.68	427,079	0.20
Private individuals	31,726,669	10.41	26,871,393	12.47
Other	20,857,923	6.84	7,350,283	3.42
Total customer accounts	**304,888,231**	**100.0**	**215,504,303**	**100.00**

NOTE 16 BALANCES DUE TO BANKS

	31.12.2012 LVL	31.12.2011 LVL
Term deposit of Pivdennyi Bank	3,440	3,440
Other interbank borrowings	1,687,293	1,176,963
	1,690,733	**1,180,403**

NOTE 17 OTHER FINANCIAL LIABILITIES

Liabilities in clearance	2,808,226	1,490,360
Settlements on behalf of a closed bank	11,656	11,656
VAT settlements	-	1,894
Cash in transit	74,820	-
Creditors settlements	74,185	120,792
	2,968,887	**1,624,702**

NOTE 18 DEFERRED INCOME AND ACCRUED EXPENSES

Accrued annual leave expenses	140,511	206,544
Accrual for guarantee fund and FCMC financing	257,110	101,771
State social security contributions to be paid	35,415	46,733
Accrued commission expenses	149,913	36,241
Other accrued expenses	78,542	122,699
	661,491	**513,988**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 19 DEFERRED INCOME TAX

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

	2012 LVL	2011 LVL
Deferred income tax (asset) / liability at the beginning of the reporting year	(6,628)	2,758
Deferred income tax change during the reporting year (see Note 8)	13,577	(9,386)
Deferred tax (asset) / liability at the end of the reporting year	**6,949**	**(6,628)**

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:

	31.12.2012 LVL	31.12.2011 LVL
Deferred income tax liability:		
Temporary difference on fixed assets depreciation	33,256	24,353
Deferred income tax assets:		
Temporary difference on accruals for unused annual leave	(26,307)	(30,981)
Deferred tax (asset) / liability	**6,949**	**(6,628)**

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 one set of each cash flow for another.

The Bank's credit risk represents the potential cost to replace the forward contracts if counterparties fail to perform their obligation. To control the level of credit risk taken, the Bank assesses counterparties using the same techniques as for its lending activities.

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

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 20 DERIVATIVE FINANCIAL INSTRUMENTS (continued)

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

	31.12.2012			31.12.2011		
	Contract / notional amount	Fair value		Contract / notional amount	Fair value	
		Assets	Liabilities		Assets	Liabilities
Currency swaps	26,582,699	110,680	(150,636)	14,617,929	251,231	(232,258)
Currency forwards	2,934,947	1,957	(6,583)	6,985,160	42,596	(8,281)
Total		**112,637**	**(157,219)**		**293,827**	**(240,539)**

The table below allocates the Bank’s derivative instruments future cash flows as at 31 December 2012:

	Up to 1 month LVL	1 to 3 months LVL	Over 3 months LVL	Total LVL
Derivatives settled on a gross basis				
Foreign exchange derivatives:				
- inflow	29,135,716	-	527,103	29,662,819
- outflow	(29,196,938)	-	(510,556)	(29,707,494)

The table below allocates the Bank’s derivative instruments future cash flows as at 31 December 2011:

	Up to 1 month LVL	1 to 3 months LVL	Over 3 months LVL	Total LVL
Derivatives settled on a gross basis				
Foreign exchange derivatives:				
- inflow	20,939,046	801,394	-	21,740,440
- outflow	(20,903,627)	(784,215)	-	(21,687,842)

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 21 SHARE CAPITAL

Issued and fully paid share capital as at 31 December 2012 was LVL 22,725,000 (2011: LVL 11,125,000).

On 27 February 2012 Shareholders meeting decided to increase Bank's share capital by LVL 6.4 million by issuing 6.4 million shares with a nominal value of LVL 1. Selling price - LVL 1 per share. The right to purchase 4.3 million shares was exercised by current shareholder Pivdennyi Bank. The rights to purchase remaining amount – 2.1 million shares were exercised by Chairman of the Council Iurii Rodin. A payment for the subscribed shares was made by Iurii Rodin and Pivdennyi Bank on 27 April 2012. The Company Register accepted the decision about increase of share capital on 28 April 2012.

On 16 April 2012 the shareholder Fortum Trade Services sold all of its shares in the amount of 900,000 to Drawnex Universal S.A.

On 26 June 2012 Shareholders meeting decided to increase Bank's share capital by LVL 200,000 by issuing 200,000 shares with a nominal value of LVL 1. Selling price - LVL 1 per share. On 13 August 2012 during Board meeting it was decided to amend conditions about increasing of share capital approved by Board on 26 June 2012. According to amendments made, share capital was increased by 5.2 million LVL. The right to purchase 5 million shares was exercised by current shareholder Pivdennyi Bank. The rights to purchase remaining amount – 200 thousand shares were exercised by third party Oleg Atayants. Payments for the subscribed shares were made by Pivdennyi Bank and Oleg Atayants on 11 December and 26 November 2012 accordingly.

As at 31 December 2012 the share capital consists of 22,725,000 ordinary shares with the nominal value of LVL 1 per share of which 22,725,000 were shares with voting rights with a total nominal value of LVL 22,725,000.

As at 31 December 2012 and 31 December 2011 the Bank's shareholders were as follows:

	31.12.2012		**31.12.2011**	
	Paid-in share capital LVL	**% of total paid-in capital %**	**Paid-in share capital LVL**	**% of total paid-in capital %**
Pivdennyi Bank	18,599,670	81.85	9,299,670	83.59
Iurii Rodin	2,100,000	9.24	-	-
DrawNex Universal S.A	900,000	3.96	-	-
Fortum Trade Services LTD	-	-	900,000	8.09
Aztin corporation	500,000	2.20	500,000	4.50
Oleg Atayants	200,000	0.88	-	-
Vitalii Medvedchuk	200,000	0.88	200,000	1.80
Oleksandr Tambovtsev	200,000	0.88	200,000	1.80
Iryna Veselukha	25,000	0.11	25,000	0.22
Haralds Abolins	220	-	110	-
Oleksandr Kuperman	-	-	110	-
Daiga Muravska	110	-	110	-
	22,725,000	**100.00**	**11,125,000**	**100.00**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 22 COMMITMENTS AND CONTINGENT LIABILITIES

Contingent liabilities

The following table discloses contingent liabilities:

	31.12.2012 LVL	31.12.2011 LVL
Warranties	6,016,694	4,991,407
	6,016,694	**4,991,407**

The Bank has issued warranties in the amount of LVL 6,016,694. These warranties are secured by deposits placed with the Bank or money resources in the security accounts.

Financial commitments

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

	31.12.2012 LVL	31.12.2011 LVL
Letters of credit	1,073,834	1,006,997
Commitments for trade cheques	325,996	381,619
Loans	17,770,705	12,014,053
	19,170,535	**13,402,669**

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

Loan commitments	17,075,558	11,396,580
Undrawn credit lines	695,147	617,473
Total lending commitments	**17,770,705**	**12,014,053**

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 lending commitments are denominated in the following currencies:

	31.12.2012 LVL	31.12.2011 LVL
USD	12,588,045	7,598,789
EUR	1,504,969	2,556,241
Other currencies	3,677,691	1,859,023
Total	**17,770,705**	**12,014,053**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 22 COMMITMENTS AND CONTINGENT LIABILITIES (continued)

Commitment under operating lease agreement

The Bank has entered into an operating lease agreement for its office premises. The lease agreement expires in June 2025. The non-cancellable lease liabilities payable within a year are LVL 308,344.

Where the Bank is the lessee, the future lease payments under concluded operating lease agreements are as follows:

	31.12.2012 LVL	31.12.2011 LVL
Up to 1 year	296,670	308,344
1 to 5 years	1,662,863	1,792,170
Over 5 years	2,710,821	3,093,146
Total	**4,670,354**	**5,193,660**

Assets pledged and restricted

As at year 2012 and 2011 the Bank had the following assets pledged:

	2012		2011	
	Assets pledged	**Related liabilities**	**Assets pledged**	**Related liabilities**
Loans and advances to customers	2,840,850	-	2,720,000	-
Total	**2,840,850**	**-**	**2,720,000**	**-**

NOTE 23 CASH AND CASH EQUIVALENTS

	31.12.2012 LVL	31.12.2011 LVL
Cash and balances on demand with the Bank of Latvia	44,440,857	11,880,259
Due from banks with original maturity of 3 months or less	184,287,449	118,801,097
Due to banks with original maturity of 3 months or less	(1,690,733)	(1,180,403)
Total	**227,037,573**	**129,500,953**

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 2012 has been set in the table below:

Description	**31.12.2012 LVL**
Tier 1	
- paid-in share capital	22,725,000
- audited retained earnings	1,417,546
- profit for the year	1,553,425
- intangible assets	(148,716)
Total Tier 1	**25,547,255**
Tier 2	
- subordinated capital	4,421,106
Total Tier 2	**4,421,106**
Capital base	**29,968,361**
Total capital requirements for credit and counterparty credit risks	
- standardised approach (SA)	9,268,980
Total capital requirement for position and foreign exchange risks	**613,328**
Total capital requirements for operational risk	
Basic index approach	881,978
Surplus of own funds	**19,204,075**
Total capital requirement	**10,764,286**
Capital adequacy ratio (%) *([Capital base]: [Capital requirement] x 8%)*	**22.27%**

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 items outstanding as at 31 December 2012 by currency profile:

	USD LVL	EUR LVL	LVL LVL	Other LVL	Total LVL
Assets					
Cash and deposits with the Bank of Latvia	198,357	30,572,601	13,669,771	128	44,440,857
Balances due from banks	187,007,901	17,531,298	57,137	2,785,466	207,381,802
Loans and advances to customers	47,443,115	18,389,305	6,997,888	-	72,830,308
Financial assets at fair value through profit or loss	2,179,033	2,691,566	9,035,960	-	13,906,559
Intangible assets	-	-	148,716	-	148,716
Property and equipment	-	-	225,108	-	225,108
Other assets	477,635	213,009	139,497	716,134	1,546,275
Total assets	**237,306,041**	**69,397,779**	**30,274,077**	**3,501,728**	**340,479,625**
Liabilities and equity					
Balances due to banks	18,493	-	1,672,240	-	1,690,733
Due to customers	243,831,287	54,456,109	4,464,574	2,136,261	304,888,231
Other liabilities	2,707,076	406,025	497,242	26,984	3,637,327
Derivative financial instruments	-	-	157,219	-	157,219
Subordinated loan	4,423,721	-	-	-	4,423,721
Equity	-	-	25,682,394	-	25,682,394
Total liabilities and equity	**250,980,577**	**54,862,134**	**32,473,669**	**2,163,245**	**340,479,625**
Net long / (short) position on balance sheet	**(13,674,536)**	**14,535,645**	**(2,199,592)**	**1,338,483**	**-**
Off-balance sheet claims arising from foreign exchange					
Balances due from foreign exchange	20,223,321	6,711,778	2,727,720	-	29,662,819
Liabilities from foreign exchange	6,401,895	20,451,596	2,500,000	354,003	29,707,494
Net long / (short) position on foreign exchange	**13,821,426**	**(13,739,818)**	**227,720**	**(354,003)**	**(44,675)**
Net long / (short) position	**146,890**	**795,827**	**(1,971,872)**	**984,480**	**(44,675)**
As at 31 December 2011					
Total assets	**166,446,013**	**43,968,121**	**23,687,771**	**2,975,236**	**237,077,141**
Total liabilities and shareholders' equity	**176,740,707**	**41,573,970**	**17,243,083**	**1,519,381**	**237,077,141**
Net long / (short) position on balance sheet	**(10,294,694)**	**2,394,151**	**6,444,688**	**1,455,855**	**-**

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 2012 based on the time remaining from the balance sheet date to the contractual maturity dates:

	Overdue	Within 1 month	1 – 3 months	3 – 6 months	6 –12 months	1–5 years	Over 5 years and undated	Total
	LVL	LVL	LVL	LVL	LVL	LVL	LVL	LVL
Assets								
Cash and balances with the Bank of Latvia	-	44,440,857	-	-	-	-	-	**44,440,857**
Balances due from banks	-	184,287,450	21,223	13,806,000	8,098,929	1,168,200	-	**207,381,802**
Loans and advances to customers	-	10,849,714	4,654,247	11,538,856	22,669,462	22,684,641	433,388	**72,830,308**
Financial assets at fair value through profit or loss	-	13,793,922	-	-	-	-	-	**13,793,922**
Intangible assets	-	-	-	-	-	148,716	-	**148,716**
Property and equipment	-	-	-	-	-	-	225,108	**225,108**
Derivative financial instruments	-	112,637	-	-	-	-	-	**112,637**
Next period expenses	-	-	-	-	68,459	-	-	**68,459**
Other assets	-	1,477,816	-	-	-	-	-	**1,477,816**
Total assets	**-**	**254,962,396**	**4,675,470**	**25,344,856**	**30,836,850**	**24,001,557**	**658,496**	**340,479,625**
Liabilities and equity								
Balances due to banks	-	1,690,733	-	-	-	-	-	**1,690,733**
Due to customers	-	256,668,890	6,161,215	5,349,559	17,224,087	19,484,480	-	**304,888,231**
Derivative financial instruments	-	157,219	-	-	-	-	-	**157,219**
Deferred income and accrued expenses	-	661,491	-	-	-	-	-	**661,491**
Other liabilities	-	2,975,836	-	-	-	-	-	**2,975,836**
Subordinated loan	-	2,615	-	-	-	-	4,421,106	**4,423,721**
Equity	-	-	-	-	-	-	25,682,394	**25,682,394**
Total liabilities and equity	**-**	**262,156,784**	**6,161,215**	**5,349,559**	**17,224,087**	**19,484,480**	**30,103,500**	**340,479,625**
Net liquidity		*(7,194,388)*	*(1,485,745)*	*19,995,297*	*13,612,763*	*4,517,077*	*(29,445,004)*	-
As at 31 December 2011								
Total assets	**2,968,717**	**143,864,707**	**7,136,607**	**17,615,764**	**31,169,999**	**33,643,295**	**678,052**	**237,077,141**
Total liabilities and equity	**-**	**166,653,619**	**14,790,082**	**10,327,046**	**13,109,963**	**14,183,225**	**18,013,206**	**237,077,141**
Net liquidity	*2,968,717*	*(22,788,912)*	*(7,653,475)*	*7,288,718*	*18,060,036*	*19,460,070*	*(17,335,154)*	-

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 financial liabilities on undiscounted cash flow bases as at 31 December 2012:

	Overdue	Within 1 month	1 – 3 months	3 – 6 months	6 –12 months	1–5 years	Over 5 years and undated	Total
	LVL	LVL	LVL	LVL	LVL	LVL	LVL	LVL
Balances due to banks	-	1,707,100	24,603	37,947	76,727	609,233	410,325	2,865,935
Due to customers	-	256,946,482	6,438,393	5,797,751	17,924,577	20,637,954	70,623	307,815,780
Other liabilities	-	2,975,836	-	-	-	-	-	2,975,836
Subordinated loan	-	12,793	20,355	30,532	61,065	488,520	4,616,189	5,229,454
Total liabilities	**-**	**261,642,211**	**6,483,351**	**5,866,230**	**18,062,369**	**21,735,707**	**5,097,137**	**318,887,005**

The table below allocates the Bank's financial liabilities on undiscounted cash flow bases as at 31 December 2011:

	Overdue	Within 1 month	1 – 3 months	3 – 6 months	6 –12 months	1–5 years	Over 5 years and undated	Total
	LVL	LVL	LVL	LVL	LVL	LVL	LVL	LVL
Balances due to banks	-	1,180,403	-	-	-	-	-	1,180,403
Due to customers	-	163,757,736	14,962,673	10,587,739	13,261,199	15,331,078	-	217,900,425
Other liabilities	-	1,865,241	-	513,988	-	-	-	2,379,229
Subordinated loan	-	13,600	27,200	179,520	220,320	1,806,080	6,175,291	8,422,011
Total liabilities	**-**	**166,816,980**	**14,989,873**	**10,767,259**	**13,995,507**	**17,137,158**	**6,175,291**	**229,882,068**

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 2012 based on the time remaining from the balance sheet date to the earlier of maturity and contractual re-pricing dates:

	Within 1 month	**1–3 months**	**3–6 months**	**6–12 months**	**1–5 years**	**Over 5 years**	**Positions which are not sensitive to the interest rate risk**	**Total**
	LVL	**LVL**	**LVL**	**LVL**	**LVL**	**LVL**	**LVL**	**LVL**
Assets								
Cash and balances with the Bank of Latvia	-	-	-	-	-	-	44,440,719	**44,440,719**
Balances due from banks	132,852,386	-	13,806,000	-	-	-	60,443,967	**207,102,353**
Loans and advances to customers	10,681,934	7,841,500	15,145,892	21,903,048	16,863,838	145,627	-	**72,581,839**
Financial assets at fair value through profit or loss	1,999,760	2,580,049	533,732	-	7,641,948	1,032,859	5,574	**13,793,922**
Intangible assets	-	-	-	-	-	-	148,716	**148,716**
Property and equipment	-	-	-	-	-	-	225,108	**225,108**
Deferred tax expenses	-	-	-	-	-	-	-	**-**
Other assets	-	-	-	-	-	-	2,186,968	**2,186,968**
Total assets	**145,534,080**	**10,421,549**	**29,485,624**	**21,903,048**	**24,505,786**	**1,178,486**	**107,451,052**	**340,479,625**
Liabilities								
Balances due to banks	-	-	-	-	-	-	1,690,733	**1,690,733**
Due to customers	45,859,531	4,525,572	4,117,146	9,032,803	15,626,425	-	225,238,887	**304,400,364**
Other liabilities	-	-	-	-	-	-	4,285,028	**4,285,028**
Subordinated loan	-	-	-	-	-	4,421,106	-	**4,421,106**
Total liabilities	**45,859,531**	**4,525,572**	**4,117,146**	**9,032,803**	**15,626,425**	**4,421,106**	**231,214,648**	**314,790,282**
Equity							25,682,394	**25,682,394**
Total liabilities and equity	**45,859,531**	**4,525,572**	**4,117,146**	**9,032,803**	**15,626,425**	**4,421,106**	**256,897,042**	**340,479,625**
On balance sheet interest sensitivity analysis	*99,674,549*	*5,895,977*	*25,368,478*	*12,870,245*	*8,879,361*	*(3,242,620)*	*(149,445,990)*	*-*
As at 31 December 2011 Total assets	**126,296,936**	**11,091,901**	**11,869,005**	**27,941,971**	**31,425,236**	**752,062**	**27,700,030**	**237,077,141**
Total liabilities and equity	**40,924,946**	**6,390,172**	**3,844,760**	**10,720,847**	**14,179,693**	**5,440,000**	**155,576,723**	**237,077,141**
On balance sheet interest sensitivity analysis	*85,371,990*	*4,701,729*	*8,024,245*	*17,221,124*	*17,245,543*	*(4,687,938)*	*(127,876,693)*	*-*

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 associated companies.

The balances in respect of operations with related parties are as follows as at 31 December 2012:

	Enterprises under the control of related parties	**Other related parties**
Undrawn credit lines	**53**	**5,414**

Total amounts of loan commitments issued to and repaid by related parties during 2012 are as follows:

	Shareholders with significant control	**Enterprises under the control of related parties**	**Other related parties**
Issued to related parties	14,973,544,949	-	82,258
Repaid by related parties	14,913,600,363	-	85,341

Operations with the related parties were as follows as at 31 December 2012:

	Shareholders with significant control	**Enterprises under the control of related parties**	**Other related parties**
Total loans and advances (interest rate on agreement: 2-24%)	83,609,478	1,844,719	20,576
Correspondent account	2,699,528	-	-
Due to customers (interest rate: 3.65 – 8.5%)	-	13,185,884	1,373,238
Derivative financial instruments	1,343	-	-
Subordinated loan	1,766,523	-	-
Vostro account	3,440	-	-

Income and expense from operations with related parties during 2012 were as follows:

	Shareholders with significant control	**Enterprises under the control of related parties**	**Other related parties**
Interest income	6,000,315	154,966	1,226
Interest expenses	(286,764)	(422,339)	(60,422)
Fee and commission income	-	541	601
Fee and commission expense	(6,156)	-	-
Administrative and other operating expenses	(15,819)	-	-

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 28 RELATED PARTY TRANSACTIONS (continued)

The balances in respect of operations with related parties are as follows as at 31 December 2011:

	Enterprises under the control of related parties	**Other related parties**
Undrawn credit lines	**54**	**13,893**

Total amounts of loan commitments issued to and repaid by related parties during 2011 are as follows:

	Shareholders with significant control	**Enterprises under the control of related parties**	**Other related parties**
Issued to related parties	3,509,395,404	1,768,350	57,179
Repaid by related parties	3,497,324,441	-	54,412

Operations with the related parties were as follows as at 31 December 2011:

	Shareholders with significant control	**Enterprises under the control of related parties**	**Other related parties**
Total loans and advances (interest rate on agreement: 6-24%)	25,524,325	1,888,582	23,855
Correspondent account	3,972,875	-	-
Due to customers (interest rate: 4.5 – 7.5%)	3,292,515	2,311,145	1,752,068
Vostro account	3,440	-	-

Income and expense from operations with related parties during 2011 were as follows:

	Shareholders with significant control	**Enterprises under the control of related parties**	**Other related parties**
Interest income	1,745,802	21,318	989
Interest expenses	(27,876)	(117,640)	(94,148)
Fee and commission income	-	211	1,066
Fee and commission expense	(6,204)	-	-
Administrative and other operating expenses	(15,920)	-	-

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 28 RELATED PARTY TRANSACTIONS (continued)

Remuneration to key management personnel is disclosed below:

	2012 LVL	2011 LVL
Short-term benefits:		
- Salaries	209,249	230,357
Pension benefits:		
- Expenses to the State Pension Insurance	50,029	55,493
Total	**259,278**	**285,850**

NOTE 29 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES

In respect of financial assets and liabilities held in the balance sheet at carrying values other than fair value, in the opinion of Management the fair value of those financial assets and liabilities differ from their carrying values, as follows:

	2012		2011	
	Book value LVL	Fair value LVL	Book value LVL	Fair value LVL
Assets				
Loans to customers	**72,830,309**	**79,699,527**	**83,836,244**	**91,937,705**

Interest rates used to determine fair value are equal with the interest rates set in the loan agreements where variable part of the interest rate is calculated based on the interbank market (EURIBOR, LIBOR, etc.) rates implicit at the year end.

NOTE 30 TAXES

	Balance 31.12.2011 LVL	Calculated in 2012 LVL	Returned from the budget LVL	Transfer to another tax LVL	Paid in 2012 LVL	Balance 31.12.2012 LVL
Corporate income tax*	(358,892)	892,799	-	321,000	(854,907)	-
State compulsory social insurance contributions	46,733	591,138	-	(189,000)	(448,871)	-
Personal income tax	(1,813)	496,551	-	(132,000)	(364,525)	(1,787)
Value added tax	1,894	(50,687)	8,145	-	(3,616)	(44,264)
(Overpaid)	**(360,705)**					**(46,051)**
Liabilities	**48,627**					**-**

* CIT calculated and paid includes the amount of tax withheld abroad – LVL 816,577.

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

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 31 SUBORDINATED LOAN

On 23 August 2011 Bank signed an agreement with Venture Resource Investments LTD receiving subordinated loan in amount of USD 2,000,000 maturing in 2019. At 31 December 2012 interest rate for subordinated loan was 8%.

On 22 November 2011 Bank signed an agreement with Pivdennyi Bank receiving subordinated loan in amount of USD 6,000,000 maturing in 2018. On 27 April 2012 after receiving of approval from FCMC the agreement was cancelled and all resources were used in the increase of Bank's share capital for the amount LVL 4,300,000.

On 9 December 2011 Bank signed an agreement with Aleksey Fedorichev receiving subordinated loan in amount of USD 2,000,000 maturing in 2018. As at 31 December 2012 interest rate for subordinated loan was 7%.

On 8 June 2012 Bank signed an agreement with Fortum Trade Services LTD receiving subordinated loan in amount of USD 1,000,000 maturing in 2019. As at 31 December 2012 interest rate for subordinated loan was 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. As at 31 December 2012 the balance of the subordinated loan of Pivdennyi Bank comprise USD 3,326,000 maturing in 2020. As at 31 December 2012 interest rate for subordinated loan was 8.5 %.

As at 31 December 2012 subordinated loans amounted to total of LVL 4,423,721 (31.12.2011: LVL 5,470,660).

NOTE 32 SUBSEQUENT EVENTS

There are no subsequent events since the last date of the reporting year, which would have a significant effect on the financial position of the Company as at 31 December 2012.