JSC ''REGIONALA INVESTICIJU BANKA"

ANNUAL REPORT FOR THE YEAR ENDED 31 DECEMBER 2010

CONTENTS

AS “Regionala Investiciju banka”

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Report of the Management

AS „Regionala investiciju banka" (hereinafter – the Bank) can describe their actions in 2010 as cautious and more focused on the development of quality of existing services. In 2010 the number of Customers and transactions have increased, improvements into internal procedures and information technologies of the Bank have been introduced, the development of the Bulgarian branch has been continued. The Bank's assets during the year have increased by LVL 49,122,136 and on the 31 December 2010 the total amount of assets was LVL 175,313,825. In the year 2010 the income of the Bank has been affected by the reserves created, as a result, the Bank has concluded the year with a loss of LVL 116,676.

Overall economic situation

Year 2010 was marked as a stabilization year for the world's economy, during which the economic indicators of the developed countries showed positive growth rates. The economic situation in Latvia significantly improved as well, and after two years of GDP decline the country's economy returned to growth. The improvement in economic indicators of other countries during 2010 suggests that the situation in Latvia could stabilize in the next two to three years and the country could return to a moderate growth.

Last year a positive development in the country was also appreciated by the credit rating agencies – S&P even raised the Latvian government's credit rating. It should be noted that both credit rating agencies and international economic experts suggest that a positive development for the country in the future requires further reduction of budget deficit and structural reforms.

The Bank's activities are subject to trends in the Ukrainian market. Ukraine has also concluded 2010 positively – a strong economic growth is continuing which is driven by both improving economic situation in the world and the growth of domestic demand. After a long period of instability the exchange rate fluctuations have normalized and the rise of inflation is falling.

Bank's operations are also affected by trends in the Bulgarian market, where the Bank has opened a branch. Due to a significant increase in export in the 3rd quarter of 2010 the GDP in Bulgaria for the first time since the beginning of 2009 showed an increase. Although it appears that the rapid economic downturn has been suppressed, a healthy development of the country in the future is also largely dependent on the situation in Bulgaria's export markets as domestic demand remains weak.

Management believes that under current conditions it is using all available resources to ensure sustainable development of the Bank's business.

Performance of the Bank during the reporting year

During 2010 The Bank has continued to successfully attract new customers - the number of customers during the year has increased by 24%. With increasing number of customers, the volumes of customers' transactions increased as well. For example, payment card transactions, in comparison with 2009, increased by 48%. In 2010 there was an increase both in outgoing and incoming number of transfers, especially in lats - the incoming number of transactions has increased by 88% and outgoing transfers - by 56%. Customer loyalty to Bank is also characterized by the fact that the deposit portfolio during the year has increased by 44%, reaching LVL 157,647,192. By contrast, given the fact that in 2010 significant provisions for problematic loans were made, the Bank's loan portfolio during the year decreased by 10%.

The Bank has made significant improvements in its payment card product where it introduced DDA chip credit cards, which provide an additional transaction security. All payment card products were redesigned so as to match the "MasterCard Worldwide" requirements. The application process for SMS Banking services for client has been alleviated – in the future the customers will be able to do it not only in the Bank but also via Internet Bank. In 2010 a cooperation agreement with AS „DnBNord Bank" has been signed for offering POS (Point of Sale) terminals to the Customers of the Bank resident in Latvia.

On 1 April 2010 the Bank has become a member of all of the NASDAQ OMX Baltic Stock Exchanges, thereby improving quality of transactions with the Customers' shares and bonds in the Baltic stock exchange markets.

In order to improve the transfer speed and quality, in 2010 a new USD currency correspondent account was opened in U.S.A. that will ensure more effective non-cash transactions.

Report of the Management (continued)

In order to optimize the Bank's internal work processes, the Bank's information technologies were improved by enhancing the range of services of the Internet Bank as well as improving the Bank's accounting system. In 2010 the Bulgarian branch started to offer Internet banking to their customers so they are able to easily manage their funds remotely.

During the year, the Bank established two new departments - Branch Coordination Unit and Debt Collection Department. Five new staff members were recruited and as a result at the end of the year 2010 the number of employees in the Bank reached 110.

In the Bulgarian branch of the Bank the management focused its efforts on attracting credit customers. To give customers service of the highest quality, administrative procedures were arranged and adapted to the Bank's standards.

Future plans and perspectives

At the beginning of 2011 the Bank is planning to increase the equity by issuing shares in the amount of LVL 4,15 million.

The emphasis during the next year will be on the increase of the credit portfolio. In order to optimize cash concentration in the correspondent accounts, the Bank intends to invest more funds into short-term U.S. government debt securities, that would signify credit risk reduction.

In 2011 the Bank intends to continue the improvement of the services for payment cards by introducing a new payment card World Signia, as well as enabling clients to apply for cards via the Internet Bank.

Early next year it is planned to introduce a new accounting system that will improve the Accounting and Personnel records and processing, as well as continue improving the Internet bank by supplementing it with an option for customers to create regular payment templates. In 2011 it is also planned to complete a new web page for the Bank.

Bulgarian branch will continue to work with attracting new clients, with an emphasis on lending and increasing the foreign exchange transfers.

Haralds Āboliņš
Chairman of the Board, President

Jurijs Rodins
Chairman of the Council

Riga, 9 March 2011

THE SUPERVISORY COUNCIL AND THE BOARD OF DIRECTORS OF THE BANK

As at 31 December 2010 and as at the date of signing the accounts:

The Council

		Date of appointment
Jurijs Rodins	Chairman of the Council	Re-elected – 31.08.2009
Marks Bekkers	Deputy Chairman of the Council	Re-elected – 31.08.2009
Dmitrijs Bekkers	Member of the Council	Re-elected – 31.08.2009
Vadims Morohovskis	Member of the Council	Re-elected – 31.08.2009
Arkādijs Fjodorovs	Member of the Council	Re-elected – 31.08.2009
Alla Vanecjancs	Member of the Council	Re-elected – 31.08.2009

The Board

Haralds Āboliņš	Chairman of the Board and President	Re-elected – 31.08.2009
Oleksandr Kuperman	Member of the Board	Re-elected – 31.08.2009
Daiga Muravska	Member of the Board	Re-elected – 31.08.2009

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 55 are prepared in accordance with the source documents and present fairly the financial position of the Bank as at 31 December 2010 and the results of its operations and cash flows for the reporting year 2010.

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 Āboliņš Chairman of the Board, President	Jurijs Rodins Chairman of the Council

Riga, 9 March 2011

Auditors' report

pwc

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 55 of AS Reģionālā Investīciju banka which comprise the statement of financial position as of 31 December 2010 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 2010, 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 2010.

PricewaterhouseCoopers SIA
Certified audit company
Licence No. 5

Ahmed Abu Sharkh
Chairman of the Board

Terēze Labzova
Certified auditor in charge
Certificate No. 184

Riga, Latvia
9 March 2011

* 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.

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Statement of Comprehensive Income for the year ended 31 December 2010

	Notes	2010 LVL	2009 LVL
Interest income	5	8,458,494	9,085,135
Interest expense	5	(5,628,079)	(5,258,470)
Net interest income		**2,830,415**	**3,826,665**
Provisions for loan impairment	11	(1,858,033)	(2,262,846)
Net interest income after provision for loan impairment		**972,382**	**1,563,819**
Fee and commission income	6	2,802,937	2,252,725
Fee and commission expense	6	(778,846)	(590,128)
Net fee and commission income	6	**2,024,091**	**1,662,597**
Profit/ (Loss) on securities trading, net		44,902	(67,693)
Profit from revaluation of securities at fair value through profit and loss account		369,350	393,387
Loss on derivative financial instruments revaluation		(15,946)	(142,369)
Profit on operation with foreign exchange, net		338,993	444,099
Profit from revaluation of foreign exchange, net		150,156	158,828
Other operating income		48,600	13,954
Administrative expense	7	(3,568,506)	(3,390,585)
Amortisation and depreciation charge	13, 14	(279,570)	(264,668)
Other operating expense		(60,964)	(55,679)
Profit before income tax		**23,488**	**315,690**
Income tax expense	8	-	-
Amount of tax paid abroad	8	(150,175)	(257,267)
Deferred income tax	8	10,011	(4,870)
Net profit/ (loss) for the year		**(116,676)**	**53,553**
Total comprehensive income/ (loss) for the year attributable to the shareholders of the Bank		**(116,676)**	**53,553**

The financial statements on pages 8 to 55 have been approved by the Supervisory Council and the Board of Directors of the Bank and signed on their behalf by:

Haralds Āboliņš
Chairman of the Board, President

Jurijs Rodins
Chairman of the Council

Riga, 9 March 2011

The accompanying notes on pages 12 to 55 are an integral part of these financial statements.

Statement of Financial Position as at 31 December 2010

	Notes	31.12.2010 LVL	31.12.2009 LVL
Assets			
Cash and balances with the Bank of Latvia	9	11,147,052	6,665,204
Balances due from banks	10	91,335,467	40,265,263
Loans and advances to customers	11	60,272,180	67,548,207
Financial assets at fair value through profit or loss	12	10,109,754	10,138,920
Derivative financial instruments	20	27,950	31,768
Intangible assets	13	382,887	461,740
Property and equipment	14	371,094	478,310
Other assets		1,180,727	202,892
Deferred expenses		110,655	98,539
Corporate income tax	30	376,059	300,846
Total assets		**175,313,825**	**126,191,689**
Liabilities			
Balances due to banks	16	1,671,699	1,682,288
Due to customers	15	157,647,192	109,233,485
Derivative financial instruments	20	55,628	43,501
Other financial liabilities	17	1,123,138	265,427
Deferred income and accrued expenses	18	409,550	433,683
Deferred income tax liability	19	2,758	12,769
Total liabilities		**160,909,965**	**111,671,153**
Equity			
Share capital	21	10,200,000	10,200,000
Retained earnings		4,320,536	4,266,983
Comprehensive income/ (loss) for the year		(116,676)	53,553
Total equity		**14,403,860**	**14,520,536**
Total liabilities and equity		**175,313,825**	**126,191,689**
Commitments and contingent liabilities			
Contingent liabilities	22	1,211,432	537,955
Financial commitments	22	18,469,844	6,619,777

The financial statements on pages 8 to 55 have been approved by the Supervisory Council and the Board of Directors of the Bank and signed on their behalf by:

Haralds Āboliņš
Chairman of the Board, President

Jurijs Rodins
Chairman of the Council

Riga, 9 March 2011

The accompanying notes on pages 12 to 55 are an integral part of these financial statements.

Statement of Changes in Equity for the year ended 31 December 2010

	Paid-in share capital	Retained earnings	Total
	LVL	LVL	LVL
Balance as at 31 December 2008	**10,200,000**	**4,266,983**	**14,466,983**
Comprehensive income for the year	-	53,553	53,553
Balance as at 31 December 2009	**10,200,000**	**4,320,536**	**14,520,536**
Comprehensive loss for the year	-	(116,676)	(116,676)
Balance as at 31 December 2010	**10,200,000**	**4,203,860**	**14,403,860**

The accompanying notes on pages 12 to 55 are an integral part of these financial statements.

Statement of Cash Flows for the year ended 31 December

	Notes	2010 LVL	2009 LVL
Cash flows from operating activities			
Interest received		6,839,296	7,805,855
Interest paid		(6,137,797)	(4,769,624)
Fees and commission received		2,802,937	2,252,725
Fees and commission paid		(778,846)	(590,128)
Income on securities trading		44,902	(67,693)
Income on foreign exchange		338,993	444,099
Other operating income		48,600	13,954
Personnel expenses paid		(2,159,252)	(1,817,501)
Administrative and other operating expenses paid		(1,470,217)	(1,628,112)
Income tax paid		(225,388)	(558,592)
Cash flows (used in)/ from operating activities before changes in operating assets and liabilities		**(696,772)**	**1,084,983**
Changes in operating assets and liabilities			
Net (increase) / decrease of securities at fair value through profit and loss account		792,609	(5,456,478)
Net (increase) / decrease of balances due from banks		(2,672,657)	14,029,824
Net (increase) / decrease of loans and advances to customers		10,685,371	(3,861,959)
Net (increase) / decrease of other assets		(989,952)	324,701
Net increase of balances due to customers		41,771,578	21,878,768
Net increase in other liabilities		833,578	88,316
Net cash and cash equivalents from operating activities		**49,723,755**	**28,088,155**
Cash flows from investing activities			
Purchase of intangible assets		(54,484)	(134,108)
Purchase of fixed assets		(39,017)	(62,332)
Net cash and cash equivalents used in financing activities		**(93,501)**	**(196,440)**
Effect of exchange rates on cash and cash equivalents		2,832,781	(994,100)
Net increase in cash and cash equivalents		**52,463,035**	**26,897,615**
Cash and cash equivalents at the beginning of the year	**23**	40,748,861	13,851,246
Cash and cash equivalents at the end of the year	**23**	**93,211,896**	**40,748,861**

The accompanying notes on pages 12 to 55 are an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 INCORPORATION AND PRINCIPAL ACTIVITIES

AS “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:
J. Alunana Street 2,
LV-1010, Riga,
Latvia

These financial statements have been approved for issue by the Supervisory Council and the Board of Directors on 8 March 2011.

NOTE 2 OPERATING ENVIRONMENT OF THE BANK

Instability in the global and Latvian financial markets and economies

Along with changes caused by the economic and financial crisis since 2008, among other things, financial markets have experienced material changes, and uncertainty in the business and investment environment has increased. Changes in the global financial markets have caused banks and other financial institutions to go bankrupt, with bank rescues being undertaken in many countries including Latvia. The recovery trend is strengthening in the global economy and the Latvian economy in 2010 has begun to grow again, however, there still remains material uncertainty about the economic development in the future.

The management believes it is taking all the necessary measures to support sustainable growth of the Bank’s business in the present circumstances.

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. The market in Latvia for many types of collateral, especially real estate, has been severely affected by the local economic slowdown resulting in there being a low level of liquidity for certain types of assets. As a result, the actual realisable 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 2009 and 2010, 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 2010 are consistent with those used in the annual financial statements for the year ended 31 December 2009, 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 2010	0.535	0.702804	0.359	0.0672
As at 31 December 2009	0.489	0.702804	0.359	0.0610

(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 to settle 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. The Bank does not designate any financial assets as 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 65% (2009: 69%) 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 200.1 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

Certain new IFRSs became effective from 1 January 2010 that are applicable for preparation of the financial statements. Listed below are those new or amended standards or interpretations which are not relevant to the Banks's daily operations or the nature of their impact on the Bank's accounting policies is insignificant.

IAS 27, Consolidated and Separate Financial Statements, revised in January 2008. The revised IAS 27 requires an entity to attribute total comprehensive income to the owners of the parent and to the non-controlling interests (previously “minority interests”) even if this results in the non-controlling interests having a deficit balance (the previous standard required the excess losses to be allocated to the owners of the parent in most cases). The revised standard specifies that changes in a parent's ownership interest in a subsidiary that do not result in the loss of control must be accounted for as equity transactions. It also specifies how an entity should measure any gain or loss arising on the loss of control of a subsidiary. At the date when control is lost, any investment retained in the former subsidiary has to be measured at its fair value.

Embedded Derivatives - Amendments to IFRIC 9 and IAS 39. The amendments clarify that on reclassification of a financial asset out of the ‘at fair value through profit or loss' category, all embedded derivatives have to be assessed and, if necessary, separately accounted for.

Eligible Hedged Items - Amendment to IAS 39. The amendment clarifies how the principles that determine whether a hedged risk or portion of cash flows is eligible for designation should be applied in particular situations.

IFRS 1, First-time Adoption of International Financial Reporting Standards, revised in December 2008. The revised IFRS 1 retains the substance of its previous version but within a changed structure in order to make it easier for the reader to understand and to better accommodate future changes.

Additional Exemptions for First-time Adopters - Amendments to IFRS 1. The amendments provide an additional exemption for measurement of oil and gas assets and also exempt entities with existing leasing contracts from reassessing the classification of those contracts in accordance with IFRIC 4, 'Determining Whether an Arrangement Contains a Lease' when the application of their national accounting requirements produced the same result.

Group Cash-settled Share-based Payment Transactions - Amendments to IFRS 2. The amendments provide a clear basis to determine the classification of share-based payment awards in both consolidated and separate financial statements. The amendments incorporate into the standard the guidance in IFRIC 8 and IFRIC 11, which are withdrawn.

IFRS 3, Business Combinations, revised in January 2008. The revised IFRS 3 allows entities to choose to measure non-controlling interests using the existing IFRS 3 method (proportionate share of the acquiree's identifiable net assets) or at fair value. The revised IFRS 3 is more detailed in providing guidance on the application of the purchase method to business combinations. The requirement to measure at fair value every asset and liability at each step in a step acquisition for the purposes of calculating a portion of goodwill has been removed. The revised IFRS 3 brings into its scope business combinations involving only mutual entities and business combinations achieved by contract alone.

IFRS 5, Non-current Assets Held for Sale and Discontinued Operations (and consequential amendments to IFRS 1). The amendment clarifies that an entity committed to a sale plan involving loss of control of a subsidiary would classify the subsidiary's assets and liabilities as held for sale. The revised guidance should be applied prospectively from the date at which the entity first applied IFRS 5.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

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

IFRIC 12, Service Concession Arrangements. The interpretation contains guidance on applying the existing standards on the contracts of a private sector representative that engages into development, financing operating or maintenance of public services, for example, private financing initiative contracts. According to these transactions, assets are recognized as intangible assets or financial assets

IFRIC 15, Agreements for the Construction of Real Estate. The interpretation applies to the accounting for revenue and associated expenses by entities that undertake the construction of real estate directly or through subcontractors, and provides guidance for determining whether agreements for the construction of real estate are within the scope of IAS 11 or IAS 18. It also provides criteria for determining when entities should recognize revenue on such transactions.

IFRIC 16, Hedges of a Net Investment in a Foreign Operation. The interpretation explains which currency risk exposures are eligible for hedge accounting and states that translation from the functional currency to the presentation currency does not create an exposure to which hedge accounting could be applied. The IFRIC allows the hedging instrument to be held by any entity or entities within a group except the foreign operation that itself is being hedged. The interpretation also clarifies how the currency translation gain or loss reclassified from other comprehensive income to profit or loss is calculated on disposal of the hedged foreign operation. Reporting entities apply IAS 39 to discontinue hedge accounting prospectively when their hedges do not meet the criteria for hedge accounting in IFRIC 16.

IFRIC 17, Distributions of Non-Cash Assets to Owners. The interpretation clarifies when and how distribution of non-cash assets as dividends to the owners should be recognised. An entity should measure a liability to distribute non-cash assets as a dividend to its owners at the fair value of the assets to be distributed. A gain or loss on disposal of the distributed non-cash assets is recognised in profit or loss for the year when the entity settles the dividend payable.

IFRIC 18, Transfers of Assets from Customers. The interpretation clarifies the accounting for transfers of assets from customers, namely, the circumstances in which the definition of an asset is met; the recognition of the asset and the measurement of its cost on initial recognition; the identification of the separately identifiable services (one or more services in exchange for the transferred asset); the recognition of revenue, and the accounting for transfers of cash from customers.

Improvements to International Financial Reporting Standards, issued in April 2009. The improvements consist of a mixture of substantive changes and clarifications in the following standards and interpretations: clarification that contributions of businesses in common control transactions and formation of joint ventures are not within the scope of IFRS 2; clarification of disclosure requirements set by IFRS 5 and other standards for non-current assets (or disposal groups) classified as held for sale or discontinued operations; requiring to report a measure of total assets and liabilities for each reportable segment under IFRS 8 only if such amounts are regularly provided to the chief operating decision maker; amending IAS 1 to allow classification of certain liabilities settled by entity’s own equity instruments as non-current; changing IAS 7 such that only expenditures that result in a recognised asset are eligible for classification as investing activities; allowing classification of certain long-term land leases as finance leases under IAS 17 even without transfer of ownership of the land at the end of the lease; providing additional guidance in IAS 18 for determining whether an entity acts as a principal or an agent; clarification in IAS 36 that a cash generating unit shall not be larger than an operating segment before aggregation; supplementing IAS 38 regarding measurement of fair value of intangible assets acquired in a business combination; amending IAS 39 (i) to include in its scope option contracts that could result in business combinations, (ii) to clarify the period of reclassifying gains or losses on cash flow hedging instruments from equity to profit or loss for the year and (iii) to state that a prepayment option is closely related to the host contract if upon exercise the borrower reimburses economic loss of the lender; amending IFRIC 9 to state that embedded derivatives in contracts acquired in common control transactions and formation of joint ventures are not within its scope; and removing the restriction in IFRIC 16 that hedging instruments may not be held by the foreign operation that itself is being hedged.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)
(bb) Adoption of new or revised standards and interpretations (continued)

Certain new standards and interpretations have been published that become effective for the accounting periods beginning on or after 1 February 2010 or later periods and which are not early adopted by the Bank.

Amendment to IAS 24, Related Party Disclosures, **issued in November 2009** (effective for annual periods beginning on or after 1 January 2011). The amended standard simplifies the disclosure requirements for government-related entities and clarifies the definition of a related party. The amendments will not have a material impact on the Bank's financial statements.

Classification of Rights Issues - Amendment to IAS 32, issued in October 2009 (effective for annual periods beginning on or after 1 February 2010). The amendment exempts certain rights issues of shares with proceeds denominated in foreign currencies from classification as financial derivatives. The amendments will not have an impact on the Bank's financial statements.

Limited exemption from comparative IFRS 7 disclosures for first-time adopters - Amendment to IFRS 1 (effective for annual periods beginning on or after 1 July 2010). Existing IFRS preparers were granted relief from presenting comparative information for the new disclosures required by the March 2009 amendments to IFRS 7 'Financial Instruments: Disclosures'. This amendment to IFRS 1 provides first-time adopters with the same transition provisions as included in the amendment to IFRS 7. The amendments will not have an impact on the Bank's financial statements.

Prepayments of a Minimum Funding Requirement – Amendment to IFRIC 14 (effective for annual periods beginning on or after 1 January 2011). This amendment will have a limited impact as it applies only to companies that are required to make minimum funding contributions to a defined benefit pension plan. It removes an unintended consequence of IFRIC 14 related to voluntary pension prepayments when there is a minimum funding requirement. The amendments will not have an impact on the Bank's financial statements.

IFRIC 19, Extinguishing Financial Liabilities with Equity Instruments (effective for annual periods beginning on or after 1 July 2010). This IFRIC clarifies the accounting when an entity renegotiates the terms of its debt with the result that the liability is extinguished through the debtor issuing its own equity instruments to the creditor. A gain or loss is recognised in the profit and loss account based on the fair value of the equity instruments compared to the carrying amount of the debt. The amendments will not have an impact on the Bank's financial statements.

Certain new standards and interpretations have been published that become effective for the accounting periods beginning on or after 1 January 2011 or later periods and which have not been endorsed by the EU:

Deferred Tax: Recovery of Underlying Assets – Amendment to IAS 12 (effective for annual periods beginning on or after 1 January 2012). The amendment introduces an exception to the existing principle for the measurement of deferred tax assets or liabilities arising on investment property measured at fair value. The amendments will not have an impact on the Bank's financial statements.

Severe hyperinflation and removal of fixed dates for first-time adopters – Amendment to IFRS 1 (effective for annual periods beginning on or after 1 July 2011). The amendments will provide relief for first-time adopters of IFRSs from having to reconstruct transactions that occurred before their date of transition to IFRSs, and guidance for entities emerging from severe hyperinflation either to resume presenting IFRS financial statements or to present IFRS financial statements for the first time. The amendments will not have an impact on the Bank's financial statements.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

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

Disclosures—Transfers of Financial Assets – Amendments to IFRS 7 (effective for annual periods beginning on or after 1 July 2011). The amendment requires additional disclosures in respect of risk exposures arising from transferred financial assets. The amendment includes a requirement to disclose by class of asset the nature, carrying amount and a description of the risks and rewards of financial assets that have been transferred to another party yet remain on the entity's balance sheet. Disclosures are also required to enable a user to understand the amount of any associated liabilities, and the relationship between the financial assets and associated liabilities. Where financial assets have been derecognised but the entity is still exposed to certain risks and rewards associated with the transferred asset, additional disclosure is required to enable the effects of those risks to be understood. The amendments will not have a material impact on the Bank’s financial statements.

IFRS 9, Financial Instruments Part 1: Classification and Measurement (effective for annual periods beginning on or after 1 January 2013). IFRS 9 issued in November 2009 replaces those parts of IAS 39 relating to the classification and measurement of financial assets. IFRS 9 was further amended in October 2010 to address the classification and measurement of financial liabilities. Key features are as follows:

- Financial assets are required to be classified into two measurement categories: those to be measured subsequently at fair value, and those to be measured subsequently at amortised cost. The decision is to be made at initial recognition. The classification depends on the entity’s business model for managing its financial instruments and the contractual cash flow characteristics of the instrument.
- An instrument is subsequently measured at amortised cost only if it is a debt instrument and both (i) the objective of the entity’s business model is to hold the asset to collect the contractual cash flows, and (ii) the asset’s contractual cash flows represent only payments of principal and interest (that is, it has only “basic loan features”). All other debt instruments are to be measured at fair value through profit or loss.
- All equity instruments are to be measured subsequently at fair value. Equity instruments that are held for trading will be measured at fair value through profit or loss. For all other equity investments, an irrevocable election can be made at initial recognition, to recognise unrealised and realised fair value gains and losses through other comprehensive income rather than profit or loss. There is to be no recycling of fair value gains and losses to profit or loss. This election may be made on an instrument-by-instrument basis. Dividends are to be presented in profit or loss, as long as they represent a return on investment.
- Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The key change is that an entity will be required to present the effects of changes in own credit risk of financial liabilities designated as at fair value through profit or loss in other comprehensive income.

The Bank is currently assessing the impact of the interpretation on its financial statements.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

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

Improvements to International Financial Reporting Standards, issued in May 2010 (effective dates vary standard by standard, most improvements are effective for annual periods beginning on or after 1 January 2011). The improvements consist of a mixture of substantive changes and clarifications in the following standards and interpretations: IFRS 1 was amended (i) to allow previous GAAP carrying value to be used as deemed cost of an item of property, plant and equipment or an intangible asset if that item was used in operations subject to rate regulation, (ii) to allow an event driven revaluation to be used as deemed cost of property, plant and equipment even if the revaluation occurs during a period covered by the first IFRS financial statements and (iii) to require a first-time adopter to explain changes in accounting policies or in the IFRS 1 exemptions between its first IFRS interim report and its first IFRS financial statements; IFRS 3 was amended (i) to require measurement at fair value (unless another measurement basis is required by other IFRS standards) of non-controlling interests that are not present ownership interest or do not entitle the holder to a proportionate share of net assets in the event of liquidation, (ii) to provide guidance on acquiree’s share-based payment arrangements that were not replaced or were voluntarily replaced as a result of a business combination and (iii) to clarify that the contingent considerations from business combinations that occurred before the effective date of revised IFRS 3 (issued in January 2008) will be accounted for in accordance with the guidance in the previous version of IFRS 3; IFRS 7 was amended to clarify certain disclosure requirements, in particular (i) by adding an explicit emphasis on the interaction between qualitative and quantitative disclosures about the nature and extent of financial risks, (ii) by removing the requirement to disclose carrying amount of renegotiated financial assets that would otherwise be past due or impaired, (iii) by replacing the requirement to disclose fair value of collateral by a more general requirement to disclose its financial effect, and (iv) by clarifying that an entity should disclose the amount of foreclosed collateral held at the reporting date and not the amount obtained during the reporting period; IAS 1 was amended to clarify that the components of the statement of changes in equity include profit or loss, other comprehensive income, total comprehensive income and transactions with owners and that an analysis of other comprehensive income by item may be presented in the notes; IAS 27 was amended by clarifying the transition rules for amendments to IAS 21, 28 and 31 made by the revised IAS 27 (as amended in January 2008); IAS 34 was amended to add additional examples of significant events and transactions requiring disclosure in a condensed interim financial report, including transfers between the levels of fair value hierarchy, changes in classification of financial assets or changes in business or economic environment that affect the fair values of the entity’s financial instruments; and IFRIC 13 was amended to clarify measurement of fair value of award credits. The amendments will not have a material impact on the Bank’s financial statements.

Unless described otherwise than above, the amendments are not expected to have material impact on the Bank’s financial statements.

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:

	31.12.2010. LVL	31.12.2009. LVL
Credit risk exposures relating to on-balance sheet assets are as follows:		
Due from credit institutions	91,335,467	40,265,263
Loans to customers	60,272,180	67,548,207
Financial assets at fair value through profit or loss	10,109,754	10,138,920
Other assets	1,180,727	202,892
Total	**162,898,128**	**118,155,282**
Credit risk exposures relating to off-balance sheet items are as follows:	1,211,432	537,955
Contingent liabilities	18,469,844	6,619,777
Financial commitments	**19,681,276**	**7,157,732**

(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 the year 2010 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:

31.12.2010.	Effect on equity		Effect on profit/loss		31.12.2009.	Effect on equity		Effect on profit/loss	
	+100 bps	-100 bps	+100 bps	-100 bps		+100 bps	-100 bps	+100 bps	-100 bps
USD	-223	223	28	-28	**USD**	-84	84	25	-25
EUR	-43	43	6	-6	**EUR**	-5	5	-3	3
LVL	122	-122	0	0	**LVL**	108	-108	1	-1
Other	0	0	0	0	**Other**	0	0	0	0
Total	**-144**	**144**	**34**	**-34**	**Total**	**19**	**-19**	**23**	**-23**

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:

31.12.2010.	Effect on equity		Effect on profit/loss		31.12.2009.	Effect on equity		Effect on profit/loss	
	+100 bps	-100 bps	+100 bps	-100 bps		+100 bps	-100 bps	+100 bps	-100 bps
Total	**-56**	**56**	**25**	**-25**	**Total**	**69**	**-69**	**9**	**-9**

(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:

31.12.2010.	Effect on equity		Effect on profit/loss		31.12.2009.	Effect on equity		Effect on profit/loss	
	+100 bps	-100 bps	+100 bps	-100 bps		+100 bps	-100 bps	+100 bps	-100 bps
USD	-241	241	678	-678	**USD**	-196	196	206	-206
EUR	-64	64	154	-154	**EUR**	-51	51	190	-190
LVL	-94	94	18	-18	**LVL**	-44	44	39	-39
Other	1	-1	-11	11	**Other**	0	0	-2	2
Total	**-398**	**398**	**839**	**-839**	**Total**	**-291**	**291**	**433**	**-433**

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

31.12.2010.	Effect on equity		Effect on profit/loss		31.12.2009.	Effect on equity		Effect on profit/loss	
	+100 bps	-100 bps	+100 bps	-100 bps		+100 bps	-100 bps	+100 bps	-100 bps
Total	**-375**	**375**	**610**	**-610**	**Total**	**-272**	**272**	**434**	**-434**

(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 2010 was 14.31%, which is above the minimum required by the FCMC since year 2004. 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). Bank’s capital adequacy ratio as at 31 December 2009 was 16.21%.

(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

	2010 LVL	2009 LVL
Interest income		
Loans and advances to legal entities	5,881,974	5,309,359
Loans and advances to private individuals	299,118	288,558
Balances due from banks	1,335,983	2,861,783
Trading securities	941,419	625,435
Total interest income	**8,458,494**	**9,085,135**
Interest expense		
Due to private individuals	(745,139)	(574,548)
Due to legal entities	(4,533,122)	(4,328,310)
Balances due to banks	(73,461)	(133,512)
Balances due to Bank of Latvia	-	(14,351)
Other liabilities	(276,357)	(207,749)
Total interest expense	**(5,628,079)**	**(5,258,470)**
Net interest income	**2,830,415**	**3,826,665**

NOTE 6 FEE AND COMMISSION INCOME AND EXPENSE

	2010 LVL	2009 LVL
Fee and commission income		
Money transfers	2,173,762	1,800,602
Loan related fees	692	365
Trust activities	-	518
Accounts servicing	204,869	102,911
Letters of credit	58,940	47,775
Sale of deposit certificates	365	7,228
Commission income on transactions with financial instruments	81,635	60,359
Commission income on current accounts	30,847	23,945
Income from general services	42,232	89,680
Other commissions (DIGIPAS)	10,811	10,889
Interbank commission income	32,956	18,598
Commission for dealing with cards	51,023	31,627
Income from currency exchange	72,047	33,542
Other income	42,758	24,686
Total fee and commission income	**2,802,937**	**2,252,725**
Fee and commission expense		
Money transfers	(673,711)	(539,236)
Other expense	(105,135)	(50,892)
Total fee and commission expense	**(778,846)**	**(590,128)**
Net fee and commission income	**2,024,091**	**1,662,597**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 7 ADMINISTRATIVE EXPENSE

	2010 LVL	2009 LVL
Remuneration paid to personnel	1,537,322	1,465,479
Rent expense	360,497	398,938
Office and equipment maintenance	88,344	108,102
Remuneration paid to the members of the Council and the Board	205,015	217,048
Security services	54,472	15,244
Public utilities	40,286	39,826
State compulsory social insurance contributions	416,591	348,072
Communication expense	225,226	200,778
Consulting and professional fees	266,559	264,100
Set-up and maintenance costs of information systems	85,171	56,899
Business trips	64,169	53,263
Introduction of credit cards	-	4,027
Transportation	32,866	49,534
Sponsorship	12,582	13,206
Health insurance	2,873	11,761
Advertising and marketing	2,629	2,328
Penalties	727	2,738
Other administrative expense	173,177	139,242
	3,568,506	**3,390,585**

The average number of staff employed by the Bank in 2010 was 105 (2009: 103).

NOTE 8 INCOME TAX EXPENSE

Corporate income tax for the reporting year	-	-
Amount of tax paid abroad	150,175	257,267
(Decrease) / increase in provisions for deferred tax liability (see Note 19)	(10,011)	4,870
Total corporate income tax	**140,164**	**262,137**

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

Profit before income tax	**23,488**	**315,690**
Theoretically calculated tax at a tax rate of 15%	3,523	47,354
Profit from revaluation of securities at fair value through profit and loss account, net	(55,403)	(59,008)
Other expenses not deductible for tax purposes	41,869	16,524
Amount of tax paid abroad	150,175	257,267
Corporate income tax expense	**140,164**	**262,137**

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

	31.12.2010 LVL	31.12.2009 LVL
Cash	909,256	592,228
Balances on demand with the Bank of Latvia	10,237,796	6,072,976
	11,147,052	**6,665,204**

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 24/12/2010 till 23/01/2011 has been set in amount of 6,920,435 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

	31.12.2010 LVL	31.12.2009 LVL
Due from Republic of Latvia credit institutions	28,227,634	734,517
Due from non-OECD credit institutions	14,788,976	16,840,076
Due from OECD credit institutions	48,318,857	22,690,670
	91,335,467	**40,265,263**

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

On demand	46,821,032	28,453,524
Balances with maturity of three months or less	36,915,510	7,312,421
Other balances due from banks	7,598,925	4,499,318
	91,335,467	**40,265,263**

The following table discloses balances due from banks according to their ratings as at 31 December 2010 and 31 December 2009:

	31.12.2010		**31.12.2009**	
Rating	**Due from banks LVL**	**%**	**Due from banks LVL**	**%**
From Aaa to Aa3	17,322,809	18.97%	9,983,336	24.79%
From A1 to A3	43,314,645	47.42%	12,583,443	31.25%
From Baa1 to Baa3	14,560,942	15.94%	830,609	2.06%
From Ba1 to Ba3	43,811	0.05%	-	0.0%
From B1 to B3	13,922,832	15.24%	16,649,289	41.35%
	89,165,039	**97.62%**	**40,046,677**	**99.45%**
Without rating	2,170,428	2.38%	218,586	0.55%
	91,335,467	**100.0%**	**40,265,263**	**100.0%**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11 LOANS AND ADVANCES TO CUSTOMERS

Analysis of loans by client type and by products

	31.12.2010 LVL	31.12.2009 LVL
Loans to legal entities	60,539,166	66,006,319
Loans to private individuals, except for mortgages	1,740,672	2,042,927
Loans to private individuals – private enterprises	61,295	60,817
Mortgages	2,953,469	2,564,843
Less: provisions for loan impairment	(5,022,422)	(3,126,699)
Total loans and advances to customers	**60,272,180**	**67,548,207**

The following table discloses changes in provisions for loan impairment during 2010

	Loans to legal entities	Loans to private individuals, except for mortgages	Mortgages	Total
Provisions for loan impairment as at 1 January 2010	**2,936,320**	**144,395**	**45,984**	**3,126,699**
Increase in provisions for loan impairment for the year	1,733,193	75,892	31,662	1,840,747
Impact of foreign currency revaluation	54,976	-	-	54,976
Provisions for loan impairment as at 31 December 2010	**4,724,489**	**220,287**	**77,646**	**5,022,422**

The following table discloses changes in provisions for loan impairment during 2009:

	Loans to legal entities	Loans to private individuals, except for mortgages	Mortgages	Total
Provisions for loan impairment as at 1 January 2009	**1,151,410**	**124**	**-**	**1,151,534**
Increase in provisions for loan impairment for the year	2,072,591	144,271	45,984	2,262,846
Impact of foreign currency revaluation	(290,138)	-	-	(290,138)
Provisions for loan impairment as at 31 December 2009	2,457	-	-	2,457
Provisions for loan impairment as at 31 December 2009	**2,936,320**	**144,395**	**45,984**	**3,126,699**

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

	2010		2009	
	LVL	%	LVL	%
Trade and commercial activities	20,424,422	31.28%	25,561,149	36.17%
Private individuals	4,694,142	7.19%	4,668,588	6.60%
Agriculture and food industry	3,057,796	4.68%	1,980,103	2.80%
Construction and operations with real estate	12,320,510	18.87%	10,334,419	14.62%
Transport and communication	9,262,404	14.19%	7,100,390	10.05%
Industry	38,315	0.06%	540,781	0.77%
Tourism and hotel services, restaurant business	3,200,188	4.9%	3,271,383	4.63%
Other	12,296,825	18.83%	17,218,093	24.36%
Loans and advances to customers (before provisions for impairment)	**65,294,602**	**100.00%**	**70,674,906**	**100.00%**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 11 LOANS AND ADVANCES TO CUSTOMERS (continued)

As at 31 December 2010, the total amount of loans issued to 10 largest clients was LVL 20,921,831 (2009: 30,489,481 LVL), which comprises 32.04% of the total credit portfolio (2009: 43.14%). As at 31 December 2010, there were no loans and advances to clients secured by deposits (2009: 5,323,740 LVL)

The following table shows the information about collateral as at 31 December 2010

	Loans to legal entities	**Loans to private individuals, except for mortgages**	**Loans to private individuals – private enterprises**	**Mortgages**	**Total**
Unsecured	829,000	171,288	-	100,758	1,101,046
Collateralised by:					
- residential real estate	4,663,583	245,765	-	769,734	5,679,082
- other real estate	43,914,838	1,293,650	-	2,012,696	47,221,184
- tradeable securities	3,090,998	-	61,295	-	3,152,293
- cash deposits	1,388,517	29,970	-	70,280	1,488,767
- other assets	6,652,230	-	-	-	6,652,230
Total loans and advances to customers	**60,539,166**	**1,740,673**	**61,295**	**2,953,468**	**65,294,602**

The following table shows the information about collateral as at 31 December 2009:

	Loans to legal entities	**Loans to private individuals, except for mortgages**	**Loans to private individuals – private enterprises**	**Mortgages**	**Total**
Unsecured	1,059,665	102,607	-	-	1,162,272
Collateralised by:					
- residential real estate	4,693,073	1,038,465		282,758	6,014,296
- other real estate	35,844,736	901,855	-	2,072,533	38,819,124
- tradeable securities	3,061,326	-	60,817		3,122,143
- cash deposits	6,136,078	-	-	209,553	6,345,631
- other assets	15,211,440	-	-	-	15,211,440
Total loans and advances to customers	**66,006,318**	**2,042,927**	**60,817**	**2,564,844**	**70,674,906**

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 2010 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	2,296,829	-	-	-	2,296,829
- Loans to medium size entities	2,229,892	-	-	-	2,229,892
- Loans to small size entities	36,124,725	-	61,295	-	36,186,020
- Loans to private individuals	-	163,785	-	2,459,469	2,623,254
Total neither past due nor impaired	**40,651,446**	**163,785**	**61,295**	**2,459,469**	**43,335,995**
Past due but not impaired					
- past due 30 days	4,286,375	-	-	-	4,286,375
- past due from 30 to 90 days	2,358,653	-	-	-	2,358,653
- past due over 360 days	401	-	-	-	401
Total past due, but not impaired	**6,645,429**	**-**	**-**	**-**	**6,645,429**
Individually impaired loans (total amount)					
- not past due	4,763,335	1,151,306	-	-	5,914,641
- past due up to 30 days	33,841	387,785	-	-	421,626
- past due 30 – 90 days	-	-	-	138,813	138,813
- past due 91 – 180 days	1,300,925	15,221	-	325,781	1,641,927
- past due 181 – 360 days	1,613,908	7,418	-	-	1,621,326
- past due over 360 days	5,530,282	15,157	-	29,406	5,574,845
Total individually impaired loans (total amount)	**13,242,291**	**1,576,887**	**-**	**494,000**	**15,313,178**
Less: provisions for loan impairment	**(4,724,490)**	**(220,286)**	**-**	**(77,646)**	**(5,022,422)**
Total loans and advances to customers	**55,814,676**	**1,520,386**	**61,295**	**2,875,823**	**60,272,180**

Loans past due, but not impaired include all amounts due from borrowers. Amount actually overdue as at 31 December 2010 were 688,705 LVL.

Loans past due and individually impaired include all amounts due from borrowers. Amount actually overdue as at 31 December 2010 was 8,666,909 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 2009 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	489,206	-	-	-	489,206
- Loans to medium size entities	5,319,736	-	-	-	5,319,736
- Loans to small size entities	49,412,290	-	60,817	-	49,473,107
- Loans to private individuals	-	864,152	-	2,025,494	2,889,646
Total neither past due nor impaired	**55,221,232**	**864,152**	**60,817**	**2,025,494**	**58,171,695**
Past due but not impaired					
- past due 30 days	1,296,924	249,096	-	318,506	1,864,526
- past due over 360 days	328	-	-	-	328
Total past due, but not impaired	**1,297,252**	**249,096**	**-**	**318,506**	**1,864,854**
Individually impaired loans (total amount)					
- not past due	3,851,351	915,092	-	138,597	4,905,040
- past due up to 30 days	177,231	-	-	45,904	223,135
- past due 30 – 90 days	12,362	-	-	-	12,362
- past due 91 – 180 days	14,308	195	-	-	14,503
- past due 181 – 360 days	81,847	14,392	-	-	96,239
- past due over 360 days	5,350,736	-	-	36,343	5,387,079
Total individually impaired loans (total amount)	**9,487,835**	**929,679**	**-**	**220,844**	**10,638,358**
Less: provisions for loan impairment	**(2,936,320)**	**(144,395)**	**-**	**(45,984)**	**(3,126,699)**
Total loans and advances to customers	**63,069,998**	**1,898,532**	**60,817**	**2,518,860**	**67,548,207**

The primary factors that the Bank considers in determining whether a loan is impaired are its overdue status and realisability 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 2010 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			
- residential real estate	261,846	-	-
- other real estate	9,450,781	-	-
- other assets	4,586,018	-	-
Fair value of collateral – individually impaired loans			
- residential real estate	1,785,333	651,549	241,000
- other real estate	21,258,068	1,803,000	565,000
- other assets	6,324,749	320,100	-
Total	**43,666,795**	**2,774,649**	**806,000**

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 2009 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			
- residential real estate	292,574	638,849	-
- other real estate	1,029,700	-	565,000
- other assets	2,869,787	-	-
Fair value of collateral – individually impaired loans			
- residential real estate	1,092,911	12,700	53,300
- other real estate	16,959,042	1,100,000	310,000
- other assets	4,366,047	933,800	-
Total	**26,610,061**	**2,685,349**	**928,300**

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 2009 and 2010.

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 12 FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT AND LOSS

	31.12.2010 LVL	31.12.2009 LVL
Latvian government securities	5,898,243	6,455,228
Non-OECD state government debt securities	2,187,407	-
Non-OECD region corporate debt securities	1,496,234	1,032,302
Latvian corporate debt securities	509,005	792,693
Unquoted securities	14,129	1,858,697
Quoted securities	4,736	-
	10,109,754	**10,138,920**

Analysis of securities by category as at 31 December 2010 and 31 December 2009 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.

	31.12.2010. LVL	31.12.2009. LVL
Category 1	10,109,754	8,280,223
Category 3	-	1,858,697
	10,109,754	**10,138,920**

Movement of securities included into Category 3 was as follows: :

	2010 LVL	2009 LVL
Category 3 at the beginning of the year	**1,858,697**	**176,107**
Purchase of securities	-	1,697,203
Sale of securities	(2,059,750)	(176,107)
Profit/ loss of the sale of securities	12,137	-
Impact of foreign currency revaluation	188,916	161,494
Category 3 at the end of the year	**-**	**1,858,697**

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 2010 and 31 December 2009:

	31.12.2010.		31.12.2009.	
Rating	**Securities**		**Securities**	
	LVL	**%**	**LVL**	**%**
From A1 to A3	-	0.00%	-	0.00%
From Baa1 to Baa3	5,898,243	58.34%	6,455,228	63.67%
From Ba1 to Ba3	509,005	5.04%	75,671	0.75%
From B1 to B3	3,052,146	30.19%	870,428	8.58%
Under B3	650,360	6.43%	496,396	4.90%
	10,109,754	**100%**	**7,897,723**	**77.90%**
Without rating	-	0.00%	2,241,197	22.10%
	10,109,754	**100%**	**10,138,920**	**100.0%**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 13 INTANGIBLE ASSETS

The following changes in the Bank's intangible assets took place during the year 2010 and 2009.

	Software 2010 LVL	Software 2009 LVL
Cost		
As at the beginning of the year	**778,745**	**644,636**
Additions	28,925	128,659
Reclassified from equipment	4,396	-
Advance payments	21,163	5,450
As at end of the year	**833,229**	**778,745**
Amortisation		
Accumulated amortisation at the beginning of the year	**317,005**	**229,827**
Charge for the year	133,337	87,178
Accumulated amortisation at the end of the year	**450,342**	**317,005**
Net book value at the beginning of the year	**461,740**	**414,809**
Net book value at the end of the year	**382,887**	**461,740**

NOTE 14 PROPERTY AND EQUIPMENT

The following changes in the Bank's property and equipment took place during the year ended 31 December 2010:

	Transport LVL	Computers LVL	Office equipment LVL	Leasehold improvements LVL	Total LVL
Cost					
31.12.2009.	**16,750**	**423,323**	**391,877**	**70,932**	**902,882**
Disposals	-	-	(529)	-	(529)
Additions	-	37,463	5,950	-	41,413
Reclassified to intangible assets	-	(4,396)	-	-	(4,396)
31.12.2010.	**16,750**	**456,390**	**397,298**	**70,932**	**941,370**
Depreciation					
31.12.2009.	**8,654**	**294,877**	**116,742**	**4,299**	**424,572**
On disposals	-	-	(529)	-	(529)
Charge for 2010	3,350	79,803	58,781	4,299	146,233
31.12.2010.	**12,004**	**374,680**	**174,994**	**8,598**	**570,276**
Net book value 31.12.2009	**8,096**	**128,446**	**275,135**	**66,633**	**478,310**
Net book value 31.12.2010	**4,746**	**81,710**	**222,304**	**62,334**	**371,094**

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 2009:

	Transport	Computers	Office equipment	Leasehold improvements	Total
	LVL	LVL	LVL	LVL	LVL
Cost					
31.12.2008.	**16,750**	**333,929**	**419,648**	**70,932**	**841,259**
Disposals	-	(729)	-	-	(729)
Additions	-	57,956	-	-	57,956
Reclassified	-	27,771	(27,771)	-	-
Advance payments	-	4,396	-	-	4,396
31.12.2009.	**16,750**	**423,323**	**391,877**	**70,932**	**902,882**
Depreciation					
31.12.2008	**5,304**	**182,681**	**59,805**	**-**	**247,790**
On disposals	-	(708)	-	-	(708)
Charge for 2009	3,350	112,904	56,937	4,299	177,490
31.12.2009	**8,654**	**294,877**	**116,742**	**4,299**	**424,572**
Net book value 31.12.2008	**11,446**	**151,248**	**359,843**	**70,932**	**593,469**
Net book value 31.12.2009	**8,096**	**128,446**	**275,135**	**66,633**	**478,310**

NOTE 15 DUE TO CUSTOMERS

(a) Analysis of groups by customers

	31.12.2010	31.12.2009
	LVL	LVL
Legal entities		
- current/ settlement accounts	120,931,910	81,629,319
- term deposits	17,952,436	18,597,348
Private individuals		
- current/ settlement accounts	4,626,591	3,398,845
- term deposits	14,136,255	5,607,973
Total customer accounts:	**157,647,192**	**109,233,485**
Sector profile:		
Private companies	133,815,420	94,719,573
Private individuals	18,762,847	9,006,818
Financial institutions	4,860,099	5,493,446
Non-profit institutions	205,117	9,918
Central government	3,709	3,730
Total customer accounts:	**157,647,192**	**109,233,485**

(b) Analysis by place of residence

Residents	21,679,848	13,368,820
Non-residents	135,967,344	95,864,665
Total customer accounts:	**157,647,192**	**109,233,485**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 15 DUE TO CUSTOMERS (continued)

During the year ended 31 December 2010 average interest rate on term deposits due to customers was 8.18 % (2009: 8.67%) and average interest rate on demand deposits was 0.05% to 2.55% (2009: from 0% to 4.5%). All deposits have fixed interest rates.

Economic sector concentration within customer accounts is as follows:

	2010		2009	
	LVL	%	LVL	%
Manufacturing	2,769,090	1.76	1,017,596	0.93
Building and real estate	3,662,871	2.32	4,610,230	4.22
Trade and commercial activities	59,606,161	37.81	41,386,853	37.89
Financial and insurance services	36,665,013	23.26	24,360,190	22.30
Transport and communications	26,470,033	16.79	23,696,605	21.69
Agriculture and food industries	821,888	0.52	261,193	0.24
Private individuals	18,762,847	11.90	9,006,818	8.25
Other	8,889,289	5.64	4,894,000	4.48
Total customer accounts	**157,647,192**	**100.0**	**109,233,485**	**100.0**

NOTE 16 BALANCES DUE TO BANKS

	31.12.2010 LVL	31.12.2009 LVL
Term deposit of bank AB „Pivdenny”	3,440	12,440
Other interbank borrowings	1,668,259	1,405,608
Accrued interest payable	-	264,240
	1,671,699	**1,682,288**

NOTE 17 OTHER FINANCIAL LIABILITIES

Liabilities in clearance	1,043,976	148,406
Settlements on behalf of a closed bank	11,656	11,656
VAT settlements	4,983	6,637
Other creditors	62,523	98,728
	1,123,138	**265,427**

NOTE 18 DEFERRED INCOME AND ACCRUED EXPENSES

Accrued annual leave expenses	198,490	157,517
Accrual for guarantee fund and FCMC financing	79,639	57,261
State social security contributions to be paid	41,144	37,920
Accrued commission expenses	2,520	110,572
Other accrued expenses	87,757	70,413
	409,550	**433,683**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 19 DEFERRED INCOME TAX

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

	2010 LVL	2009 LVL
Deferred income tax liability at the beginning of the reporting year	12,769	7,899
Deferred income tax liability (decrease) / increase during the reporting year (see Note 8)	(10,011)	4,870
Deferred tax liability at the end of the reporting year	**2,758**	**12,769**

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:

	31.12.2010 LVL	31.12.2009 LVL
Deferred income tax liability:		
Temporary difference on fixed assets depreciation	31,123	36,397
Deferred income tax assets:		
Temporary difference on accruals for unused annual leave	(28,365)	(23,628)
Deferred tax liability	**2,758**	**12,769**

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:

	31.12.2010			31.12.2009		
	Contract / notional amount	Fair value		Contract / notional amount	Fair value	
		Assets	Liabilities		Assets	Liabilities
Currency swaps	2,174,483	24,101	(51,593)	1,683,427	31,768	(43,432)
Currency forwards	2,548,380	3,849	(4,035)	247,230	-	(69)
Total		**27,950**	**(55,628)**		**31,768**	**(43,501)**

The table below allocates the Bank's derivative instruments future cash flows as at 31 December 2010:

	Up to 1 month	1 to 3 months	Over 3 months	Total
	LVL	LVL	LVL	LVL
Derivatives settled on a gross basis				
Foreign exchange derivatives:				
- inflow	3,040,367	-	-	3,040,367
- outflow	(3,068,098)	-	-	(3,068,098)

The table below allocates the Bank's derivative instruments future cash flows as at 31 December 2009:

	Up to 1 month	1 to 3 months	Over 3 months	Total
	LVL	LVL	LVL	LVL
Derivatives settled on a gross basis				
Foreign exchange derivatives:				
- inflow	1,918,391	-	-	**1,918,391**
- outflow	(1,928,925)	-	-	**(1,928,925)**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 21 SHARE CAPITAL

Issued and fully paid share capital as at 31 December 2009 and 31 December 2010 was LVL 10,200,000. The share capital consisted of 10,200,000 ordinary shares with the nominal value of LVL 1 per share of which 10,200,000 were shares with voting rights with a total nominal value of LVL 10,200,000.

As at 31 December 2009 and 31 December 2010 the Bank’s shareholders were as follows

	31.12.2010		31.12.2009	
	Paid-in share capital LVL	**% of total paid-in capital %**	**Paid-in share capital LVL**	**% of total paid-in capital %**
AB „Pivdenny” bank	9,299,670	91.18	9,299,670	91.18
Haralds Āboliņš	110	-	110	-
Daiga Muravska	110	-	110	-
Oleksandrs Kupermans	110	-	110	-
Fortum Trade Services LTD	900,000	8.82	900,000	8.82
	10,200,000	**100.00**	**10,200,000**	**100.00**

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 22 COMMITMENTS AND CONTINGENT LIABILITIES

Contingent liabilities

The following table discloses contingent liabilities:

	31.12.2010 LVL	31.12.2009 LVL
Guarantee	208,593	-
Warranties	1,002,839	537,955
	1,211,432	**537,955**

The Bank has issued warranties in the amount of LVL 1,002,839. 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.

	31.12.2010 LVL	31.12.2009 LVL
Letters of credit	767,917	39,576
Commitments for trade cheques	457,169	-
Loans	17,244,758	6,580,201
	18,469,844	**6,619,777**

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

Loan commitments	14,579,921	1,352,248
Undrawn credit lines	2,664,837	5,227,953
Total lending commitments	**17,244,758**	**6,580,201**

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:

	31.12.2010. LVL	31.12.2009. LVL
USD	13,229,496	4,339,015
EUR	3,240,871	394,975
Other currencies	774,391	1,846,211
Total	**17,244,758**	**6,580,201**

Contingent liabilities on penalties

The Latvian Competition council has begun a case on the possible breach of the Competition Law in respect of the payment card market with regards to illegal agreements on direct or indirect settlement of processes or tariffs or their settlement principles, as well as on exchange of information relating to prices or terms of sale. A possible penalty for the breach of the law is a cash penalty of up to 5 percent of the turnover for the last financial year but not less than LVL 250 for each of the involved parties. The management believes that the impact of any potential penalty would not be significant and it is not practicable to estimate it at this stage.

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 307,268.

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

	31.12.2010. LVL	31.12.2009. LVL
Up to 1 year	307,268	439,657
1 to 5 years	1,709,138	2,536,673
Over 5 years	3,478,205	5,720,167
Total	**5,494,611**	**8,696,497**

Assets pledged and restricted

As at year 2009 and 2010 the Bank had the following assets pledged:

	2010		2009	
	Assets pledged	Related liabilities	Assets pledged	Related liabilities
Loans and advances to customers	-	-	1,406,685	1,424,349
Total	**-**	**-**	**1,406,685**	**1,424,349**

NOTE 23 CASH AND CASH EQUIVALENTS

	31.12.2010 LVL	31.12.2009 LVL
Cash and balances on demand with the Bank of Latvia	11,147,052	6,665,204
Due from banks with original maturity of 3 months or less	83,736,543	35,765,945
Due to banks	(1,671,699)	(1,682,288)
Total	**93,211,896**	**40,748,861**

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 2010 has been set in the table below:

Description	31.12.2010 LVL
Tier 1	
- paid-in share capital	10,200,000
- audited retained earnings	4,320,536
- loss for the year	(116,676)
- intangible assets	(382,887)
Total Tier 1	**14,020,973**
Capital base	**14,020,973**
Total capital requirements for credit and counterparty credit risks	**6,483,828**
- standardised approach (SA)	6,483,828
Total capital requirement for position and foreign exchange risks	**563,650**
Total capital requirements for operational risk	**789,733**
– basic index approach	789,733
Surplus of own funds	**6,183,762**
Capital adequacy ratio (%) *([Capital base]: [Surplus of own funds] x 8%)*	**14,31%**

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 2010 by currency profile:

	USD LVL	EUR LVL	LVL LVL	Other LVL	Total LVL
Assets					
Cash and deposits with the Bank of Latvia	270,561	1,332,187	9,525,871	18,433	11,147,052
Balances due from banks	80,904,486	9,169,740	593	1,260,648	91,335,467
Loans and advances to customers	35,069,616	22,737,798	2,418,969	45,797	60,272,180
Financial assets at fair value through profit or loss	3,702,507	870,663	5,536,584	-	10,109,754
Intangible assets	-	6,446	376,441	-	382,887
Property and equipment	-	-	371,094	-	371,094
Other assets	625,032	372,617	684,119	13,623	1,695,391
Total assets	**120,572,202**	**34,489,451**	**18,913,671**	**1,338,501**	**175,313,825**
Liabilities and equity					
Balances due to banks	532,659	-	1,139,040	-	1,671,699
Due to customers	118,278,312	34,143,366	3,912,935	1,312,579	157,647,192
Other liabilities	1,032,179	49,995	422,677	27,837	1,532,688
Derivative financial instruments	-	-	55,628	-	55,628
Deferred income tax liability	-	-	2,758	-	2,758
Equity	-	-	14,403,860	-	14,403,860
Total liabilities and equity	**119,843,150**	**34,193,361**	**19,936,898**	**1,340,416**	**175,313,825**
Net long / (short) position on balance sheet	**729,052**	**296,090**	**(1,023,227)**	**(1,915)**	**-**
Off-balance sheet claims arising from foreign exchange					
Balances due from foreign exchange	1,746,625	386,542	-	907,200	3,040,367
Liabilities from foreign exchange	1,297,768	863,130	-	907,200	3,068,098
Net long / (short) position on foreign exchange	**448,857**	**(476,588)**	**-**	**-**	**(27,731)**
Net long / (short) position	**1,177,909**	**(180,498)**	**(1,023,227)**	**(1,915)**	**(27,731)**
As at 31 December 2009					
Total assets	**71,958,329**	**36,959,816**	**14,472,275**	**2,801,269**	**126,191,689**
Total liabilities and shareholders’ equity	**72,984,076**	**36,277,847**	**16,087,135**	**842,631**	**126,191,689**
Net long / (short) position on balance sheet	**(1,025,747)**	**681,969**	**(1,614,860)**	**1,958,638**	**-**

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 2010 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	-	11,147,052	-	-	-	-	-	**11,147,052**
Balances due from banks	-	83,736,541	-	7,392,246	174,580	32,100	-	**91,335,467**
Loans and advances to customers	4,798,857	6,913,484	4,184,749	4,278,174	14,696,248	23,365,235	2,035,433	**60,272,180**
Financial assets at fair value through profit or loss	-	10,090,888	-	-	-	-	18,866	**10,109,754**
Intangible assets	-	-	-	-	-	382,887	-	**382,887**
Property and equipment	-	-	-	-	-	-	371,094	**371,094**
Derivative financial instruments	-	27,950	-	-	-	-	-	**27,950**
Deferred expenses	-	-	-	-	110,655	-	-	**110,655**
Income tax	-	-	376,059	-	-	-	-	**376,059**
Other assets	-	1,180,727	-	-	-	-	-	**1,180,727**
Total assets	**4,798,857**	**113,096,642**	**4,560,808**	**11,670,420**	**14,981,483**	**23,780,222**	**2,425,393**	**175,313,825**
Liabilities and equity								
Balances due to banks	-	1,671,699	-	-	-	-	-	**1,671,699**
Due to customers	-	127,379,997	2,283,317	10,669,162	10,816,349	6,498,367	-	**157,647,192**
Derivative financial instruments	-	55,628	-	-	-	-	-	**55,628**
Deferred income and accrued expenses	-	-	-	-	409,550	-	-	**409,550**
Other liabilities	-	1,123,138	-	-	-	-	-	**1,123,138**
Deferred income tax liability	-	-	-	-	2,758	-	-	**2,758**
Equity	-	-	-	-	-	-	14,403,860	**14,403,860**
Total liabilities and equity	**-**	**130,230,462**	**2,283,317**	**10,669,162**	**11,228,657**	**6,498,367**	**14,403,860**	**175,313,825**
Net liquidity	*4,798,857*	*(17,133,820)*	*2,277,491*	*1,001,258*	*3,752,826*	*17,281,855*	*(11,978,467)*	-
As at 31 December 2009								
Total assets	**3,467,371**	**51,383,608**	**12,027,371**	**14,377,790**	**23,231,612**	**17,283,350**	**4,420,587**	**126,191,689**
Total liabilities and equity	**-**	**76,941,898**	**12,087,476**	**4,311,491**	**9,763,894**	**8,566,394**	**14,520,536**	**126,191,689**
Net liquidity	**3,467,371**	*(25,558,290)*	*(60,105)*	*10,066,299*	*13,467,718*	*8,716,956*	*(10,099,949)*	-

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 2010:

	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	-	1,671,699	-	-	-	-	-	1,671,699
Due to customers	-	127,424,663	2,433,272	10,836,815	11,209,070	7,220,217	-	159,124,037
Other liabilities	-	1,178,766	-	-	412,308	-	-	1,591,074
Total liabilities	**-**	**130,275,128**	**2,433,272**	**10,836,815**	**11,621,378**	**7,220,217**	**-**	**162,386,810**

The table below allocates the Bank's financial liabilities on undiscounted cash flow bases as at 31 December 2009:

	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	-	264,498	18,741	28,112	1,443,090	-	-	1,754,441
Due to customers	-	76,530,922	12,353,162	4,719,914	8,672,834	8,940,361	-	111,217,193
Other liabilities	-	308,859	69	-	509,660	-	-	818,588
Total liabilities	**-**	**77,104,279**	**12,371,972**	**4,748,026**	**10,625,584**	**8,940,361**	**-**	**113,790,222**

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 2010 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	-	-	-	-	-	-	11,146,667	**11,146,667**
Balances due from banks	78,859,112	-	1,070,000	-	-	-	11,391,021	**91,320,133**
Loans and advances to customers	11,036,107	8,344,253	7,557,004	14,346,374	18,055,225	211,176	-	**59,550,139**
Financial assets at fair value through profit or loss	-	2,533,916	608,467	1,952,328	4,766,793	229,384	18,866	**10,109,754**
Intangible assets	-	-	-	-	-	-	382,887	**382,887**
Property and equipment	-	-	-	-	-	-	371,094	**371,094**
Other assets	-	-	-	-	-	-	2,433,151	**2,433,151**
Total assets	**89,895,219**	**10,878,169**	**9,235,471**	**16,298,702**	**22,822,018**	**440,560**	**25,743,686**	**175,313,825**
Liabilities								
Balances due to banks	3,440	-	-	-	-	-	-	**3,440**
Due to customers	48,278,326	2,207,503	4,250,252	9,839,332	6,461,980	-	86,100,079	**157,137,472**
Other liabilities	-	-	-	-	-	-	3,766,295	**3,766,295**
Deferred income tax liability	-	-	-	-	-	-	2,758	**2,758**
Total liabilities	**48,281,766**	**2,207,503**	**4,250,252**	**9,839,332**	**6,461,980**	**-**	**89,869,132**	**160,909,965**
Equity	**-**	**-**	**-**	**-**	**-**	**-**	14,403,860	**14,403,860**
Total liabilities and equity	**48,281,766**	**2,207,503**	**4,250,252**	**9,839,332**	**6,461,980**	**-**	**104,272,992**	**175,313,825**
On balance sheet interest sensitivity analysis	*41,613,453*	*8,670,666*	*4,985,219*	*6,459,370*	*16,360,038*	*440,560*	*(78,529,306)*	*-*
As at 31 December 2009								
Total assets	**34,687,786**	**11,847,312**	**17,414,876**	**21,550,862**	**13,568,641**	**448**	**27,121,764**	**126,191,689**
Total liabilities and equity	**33,601,141**	**3,280,091**	**1,663,896**	**8,923,910**	**8,534,866**	**-**	**70,187,785**	**126,191,689**
On balance sheet interest sensitivity analysis	*1,086,645*	*8,567,221*	*15,750,980*	*12,626,952*	*5,033,775*	*448*	*(43,066,021)*	*-*

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 2010:

	Enterprises under the control of beneficiaries	Other related parties
Undrawn credit lines	**54**	**16,614**

Total amounts of loan commitments issued to and repaid by related parties during 2010 are as follows:

	Shareholders with significant control	Enterprises under the control of beneficiaries	Other related parties
Issued to related parties	1,000,982,272	-	6,621
Repaid by related parties	1,007,098,776	-	2,728

Operations with the related parties were as follows as at December 2010:

	Shareholders with significant control	Enterprises under the control of beneficiaries	Other related parties
Total loans and advances (interest rate on agreement: 6-24%)	11,395,064	-	21,089
Correspondent account	1,973,176	-	-
Due to customers (interest rate: 4.5 – 7.5%)	-	811,996	317,194
Vostro account	3,440	-	-

Income and expense from operations with related parties during 2010 were as follows:

	Shareholders with significant control	Enterprises under the control of beneficiaries	Other related parties
Interest income	1,296,772	38,290	1,354
Interest expenses	-	1,222	9,175
Fee and commission income	-	5,437	1,021
Fee and commission expense	8,457	-	-
Profit from revaluation of financial instruments with revaluation through profit and loss	(6,341)	-	-
Administrative and other operating expenses	12,800	-	-

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 2009:

	Other related parties
Undrawn credit lines	**22,277**

Total amounts of loan commitments issued to and repaid by related parties during 2009 are as follows:

	Shareholders with significant control	Enterprises under the control of beneficiaries	Other related parties
Issued to related parties	3,674,339,323	-	3,977
Repaid by related parties	3,678,665,207	38,880	11,258

Operations with the related parties were as follows as at December 2009:

	Shareholders with significant control	Enterprises under the control of beneficiaries	Other related parties
Total loans and advances (interest rate on agreement: 5.5 - 18%)	16,227,628	903,018	17,196
Investment securities for trading purposes	427,838	-	-
Correspondent account	33,369	-	-
Due to customers (interest rate: 6.25 – 7.7%)	-	55,764	84,738
Vostro account	12,440	-	-

Income and expense from operations with related parties during 2009 were as follows:

	Shareholders with significant control	Enterprises under the control of beneficiaries	Other related parties
Interest income	2,520,067	62,221	1,337
Interest expenses	26,162	-	1,963
Fee and commission income	-	-	949
Fee and commission expense	7,979	-	-
Profit from revaluation of financial instruments with revaluation through profit and loss	199,848	-	-
Administrative and other operating expenses	7,599	-	-

NOTES TO THE FINANCIAL STATEMENTS (continued)

NOTE 28 RELATED PARTY TRANSACTIONS (continued)

Remuneration to key management personnel is disclosed below:

	2010 LVL	2009 LVL
Short-term benefits:		
- Salaries	198,411	258,565
Pension benefits:		
- Expenses to the State Pension Insurance	47,342	61,066
Total	**245,753**	**319,631**

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:

	2010		2009	
	Book value LVL	Fair value LVL	Book value LVL	Fair value LVL
Assets				
Loans to customers	**67,618,082**	**73,555,014**	**60,356,103**	**65,189,222**

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 31.12.2009 LVL	Calculated in 2010 LVL	Paid in 2010 LVL	Balance 31.12.2010 LVL
Corporate income tax*	(300,846)	204,415	(279,628)	(376,059)
State compulsory social insurance contributions	37,920	475,157	(471,933)	41,144
Personal income tax	(863)	410,103	(410,624)	(1,384)
Value added tax	6,637	66,540	(68,194)	4,983
(Overpaid)	**(301,709)**			**(377,443)**
Liabilities	**44,557**			**46,127**

** CIT calculated and paid is reduced by the amount of tax paid abroad – LVL 150,175.

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

NOTE 31 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 2010.