

AS "Citadele banka"

Annual report

for the 6 month period
ended 31 december 2010

together with independent
auditors' report

Translation from Latvian original*

* This version of financial statements 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 financial statements takes precedence over this translation.



Citadele

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AS "Citadele banka"
Republikas laukums 2A, Riga,
LV-1010, Latvia

Phone: (371) 67010 000
Facsimile: (371) 67010 001

www.citadele.lv

Registration number: 40103303559

Citadele Bank's activity in 2010 is characterized by stability and development

Citadele Bank was founded on 30 June 2010; and launched its activities on 1 August 2010 following the successful restructuring of Parex Banka.

The aim of Citadele Bank is to become the most valuable financial group in the Baltic States; and to inspire people and companies to growth and enhancement of regional development. Regardless of the losses in banking sector during the last years in Latvia, Citadele Bank is working purposefully in order for its activity to generate profit.

2010 was the year of stabilising and building Citadele Bank's business. The Bank has worked to develop services for clients and repay funds invested in the Bank's activity by the State as soon as possible. Along with development of services in 2010, the Bank has been working at improving operational efficiency, eliminating functions that generate losses and optimising resources.

According to December 2010 public data, Citadele Bank is the largest local bank in Latvia with branch offices in other countries; it is the third largest bank in Latvia in terms of deposits (10.4% market share), the fifth largest bank according to the amount of assets (6.9% market share) and loans issued (5.2% market share). The Bank's liquidity is stable and it significantly exceeds minimum requirements.

Bank Ownership

Citadele, the Latvian Privatisation Agency and the European Bank for Reconstruction and Development signed an agreement on 30 July 2010, whereby the EBRD took a shareholding of 25 % of share capital plus 1 voting share.

The new Supervisory Board was elected on 11 August 2010. The following members were appointed – Klāvs Vasks, Juris Vaskāns, Ģirts Freibergs, Laurence Philip Adams and Geoffrey Dunn. Juris Jākobsons, a professional in the finance field and experienced in the banking sector was nominated as Chairman of the Executive Board.

The Bank's Services for Clients Re-launched

In 2010, during the first five months of its activity, the Bank re-launched and developed three main segments: services for retail customers and small and medium enterprises in our branch office network and services for large enterprises and private wealth management.

Citadele offers loan services for enterprises, paying special attention to small and medium enterprise (SME) segment. Similarly, mortgage loans, consumption loans and provision of overdraft products for retail customers are offered in Latvia, Lithuania and Estonia. In order to practice responsible lending, the Bank introduced new procedures for mortgage loans and risk assessment.

Citadele Leasing and Factoring, the Bank's subsidiary, offers leasing services in the Baltic States, and factoring services for clients in Latvia.

The Bank's subsidiary Citadele Open Pension Fund provides management of private pension plans, achieving profitability results that were among the best in Latvia.

The Citadele Life subsidiary provides life insurance with savings, and the Citadele Asset Management subsidiary provides private capital management services.

During the first five months of activity, IPAS Citadele Asset Management introduced "Investment Gold", a new product which generated larger than anticipated interest.

The Company has also received very good references from clients on the quality of the new Bank's development process.

Business Results of the Bank and Its Group in 2010

Following the restructuring process on August 1st, Citadele Bank and its subsidiaries main goals were to relaunch the activities of its businesses.

In common with the whole banking sector in Latvia, Citadele Bank finished 2010 with losses. The loss of 19.4 million Lats (the Group – 18.8 million Lats) was broadly in line with the Restructuring Plan. The major reasons for this result were due to the slower than anticipated economic upturn and prudent provisioning as expected in the Bank's plans.

Earning clients' trust was one of the most important tasks of the new Bank. From August to December 2010, over 6,000 new clients chose Citadele Bank: Citadele has acquired over 4,900 new clients in retail and SME segment in Latvia, over 350 new clients in Estonia, and more than 600 new clients in the private capital management sector.

From August until December 2010, clients' deposit portfolio with Citadele Bank increased by 5.6% or 52.4 million Lats. The Bank's loan portfolio was 691.1 million Lats (the group – 794.3 million Lats) and the amount of capital and reserves was 84 million Lats (the Group – 82 million Lats). The total amount of deposits with Citadele Bank reached 1.1 billion Lats (the Group – 1.29 billion Lats) at the end of 2010. Total assets of Citadele Bank were 1.44 billion Lats (the Group – 1.61 billion Lats) at the end of 2010, slightly exceeding the planned amount.

During the period from August until December 2010, Citadele issued 24,918 new payment cards. Turnover in American Express credit cards per client per month increased as well; turnover in American Express Gold credit cards increased by 13% and in American Express BLUE – by 16%. By focusing on its strategic alliance with American Express and maintaining a high focus on loyal credit card customers, Citadele has secured the leading position in the Latvian market for cards with attached credit limits.

Despite some reductions in interest rates, the deposit portfolio in the corporate banking sector remained stable and in fact saw some growth between August and December.

In 2010, Citadele Leasing and Factoring Ltd succeeded at decreasing its short-term liabilities by almost 27.9 million Lats, compared to 2009, and the Company plans to finish 2011 with profit.

IPAS Citadele Asset Management, the Bank's subsidiary company, finished 2010 with a profit of 420 thousand Lats which is an increase by 135% percent comparing to 2009.

3rd level pension plans offered by Citadele Open Pension Fund, the Bank's subsidiary company, have reached the highest profitability in Latvia since they were launched. As a result, the value of pension plan assets has increased by over 157 thousand Lats comparing to 2009.

AAS Citadele Life, the Bank's subsidiary, has expanded its sales channel network in 2010, reaching a twice as large the amount of new premiums than in 2009. This enabled the Company to be placed among the most rapidly developing life insurance companies in Latvia by new insurance premiums received.

Improvement of Efficiency

Along with working on business development, Citadele Bank has worked purposefully on improving efficiency of processes by optimizing resources and reducing administrative costs.

On 31 August 2010, the Bank had 1,411 active members of staff. By year end, the results of its optimisation efforts caused this number to reduce to 1,329.

In 2010, active centralization of the Bank was completed as a result of which the area necessary for archives and archive maintenance costs were reduced. Maintenance costs of branch offices have been reduced and the use of motor vehicles has seen significant optimisation.

In 2010, an IT project on data connection change for branch offices was introduced which resulted in significant decrease of data transfer costs.

Also, in 2010, the Bank has put stationary goods supply process in order by centralising placement of orders and delivery of goods. The Bank has also acquired additional income and decreased warehouse maintenance costs by selling such furniture, office equipment and other equipment in open auctions which are not necessary for ensuring the Bank's activity.

Repayment of State-Invested Funds and the Bank's Investment in Latvia's Economy

Highly appreciating the support provided by Latvian government, one of Citadele Bank's key priorities are repayment of State-invested funds within the shortest period of time possible and encouragement of Latvia's economic activity. As early as in September 2010, during the second month of its activity, Citadele Bank paid back loans made by the Ministry of Finance of the republic of Latvia totalling of 12.1 million Lats. In 2010, in five months, Citadele has paid the State 9.2 million Lats in interest payments for the support received. A further repayment of 32.8 million Lats was made earlier than scheduled in January 2011.

Citadele has invested funds in Latvia's economy in the shape of loan funds issued to enterprises. Also, it has enhanced acquisition of resources from EU structural funds in Latvia – a significant part of enterprises that Citadele has issued funding to were companies, which needed funding for implementing projects co-funded by the European Union.

Activities of Citadele Bank and its Subsidiaries Have Been Appraised Internationally

Moody's, international rating agency, rated Citadele Bank as BA3 in long-term rating in 2010. This rating is higher than the euro obligation rating B2 given to Parex Banka before Citadele launched its activity. All ratings given to Citadele Bank provide a "stable" development prognosis.

Citadele Eastern Europe Balanced Fund was acknowledged the best balanced fund in 2010 in a poll named "Best Funds in Central and Eastern European Countries" which was conducted by European business magazine Business New Europe. Standard & Poor's Fund Services announced granting "A" quality rating in fund management to Citadele's Russian Equity Fund. SPEAR'S Russia Wealth Management Awards 2010 brought forward Citadele Bank for "Best Bank in Baltic and CIS Countries in Provision of Capital Management Services for Clients in Russia" nomination. Citadele Asset Management, a subsidiary company of the Bank, was nominated for the Annual Wealth Management Prize 2011 by World Finance, an international finance journal, as the most professional wealth management company in the Baltic States.

The Bank is Developing in Order to Work With Profit

In 2011, Citadele Bank expects to move into profitability and thus increase the Bank's worth. The Bank's business results in the first quarter show positive signs – the Bank has been adjusting and renegotiating its deposit interest rates resulting in positive net interest income.

In order to facilitate economic growth of Latvia, Citadele Bank plans to issue significant funding to Latvian companies and retail customers in 2011, paying special attention to Latvian companies with local capital. In 2011, the Bank has started working on offering unique products. Citadele Bank is working purposefully in order for its activity to generate profit.



Juris Jākobsons
Chairman of the Management Board



Klāvs Vasks
Chairman of the Council

Riga,
16 May 2011

Council of the Bank

Name	Position
Klāvs Vasks	Chairman of the Council
Juris Vaskāns	Deputy chairman of the Council
Ģirts Freibergs	Member of the Council
Laurence Philip Adams	Member of the Council
Geoffrey Dunn	Member of the Council

Management Board of the Bank

Name	Position
Juris Jākobsons	Chairman of the Management Board, p.p.
Guntis Beļavskis	Member of the Management Board, p.p.
Valters Ābele	Member of the Management Board
Kaspars Cikmačs	Member of the Management Board
Philip Nigel Allard	Member of the Management Board

According to AS Citadele Banka (thereon Citadele) founder's VAS Privatizācijas Aģentūra bank's establishment resolution Juris Vaskāns, Klāvs Vasks and Andžs Ūbelis were included in the Citadele's Council and Juris Jākobsons, Guntis Beļavskis un Valters Ābele in the Management Board of the Bank. Citadele was registered in the Register of Enterprises of the Republic of Latvia on 30 June 2010. With the Bank's Council's decision date 5 July 2010 Juris Jākobsons was elected as a Chairman of the Management Board of the Bank.

A new Council of Citadele was elected in an extraordinary shareholders meeting held on 11 August 2010. The following members were elected – Klāvs Vasks, Juris Vaskāns, Ģirts Freibergs, Laurence Philip Adams and Geoffrey Dunn. With Bank's Council's resolution dated 16 August 2010 Klāvs Vasks was elected as chairman of the council and Juris Vaskāns as deputy chairman of the council.

On 15 September 2010 the Council of the Bank made a decision, effective from 21 September 2010, to expand the Executive Board by appointing two new board members – Kaspars Cikmačs and Philip Nigel Allard.

Changes in management bodies during the reporting year and until the signing of these financial statements:

Name	Position	Date of changes	Type of changes
Kaspars Cikmačs	Member of the Management Board	15.09.2010 (effective from 21.09.2010)	Appointed
Philip Nigel Allard	Member of the Management Board	15.09.2010 (effective from 21.09.2010)	Appointed
Klāvs Vasks	Chairman of the Council	11.08.2010	Appointed
Juris Vaskāns	Deputy chairman of the Council	11.08.2010	Appointed
Ģirts Freibergs	Member of the Council	11.08.2010	Appointed
Laurence Philip Adams	Member of the Council	11.08.2010	Appointed
Geoffrey Dunn	Member of the Council	11.08.2010	Appointed
Juris Vaskāns	Member of the Council	11.08.2010	Removed
Klāvs Vasks	Member of the Council	11.08.2010	Removed
Andžs Ūbelis	Member of the Council	11.08.2010	Removed
Juris Jākobsons	Chairman of the Management Board	07.07.2010	Appointed
Juris Jākobsons	Member of the Management Board	30.06.2010	Appointed
Guntis Beļavskis	Member of the Management Board	30.06.2010	Appointed
Valters Ābele	Member of the Management Board	30.06.2010	Appointed
Juris Vaskāns	Member of the Council	30.06.2010	Appointed
Klāvs Vasks	Member of the Council	30.06.2010	Appointed
Andžs Ūbelis	Member of the Council	30.06.2010	Appointed

The Management of AS Citadele Banka (hereinafter – the Bank) are responsible for the preparation of the financial statements of the Bank as well as for the preparation of the consolidated financial statements of the Bank and its subsidiaries (hereinafter – the Group).

The financial statements set out on pages 8 to 68 are prepared in accordance with the source documents and present fairly the financial position of the Bank and the Group as at 31 December 2010 and the results of their operations, changes in shareholders' equity and cash flows for the six month period then ended. The management report set out on pages 3 to 5 presents fairly the financial results of the reporting period and future prospects of the Bank and the Group.

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

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

A handwritten signature in black ink, appearing to be 'Juris Jākobsons', written over a horizontal line.

Juris Jākobsons
Chairman of the Management Board

A handwritten signature in black ink, appearing to be 'Klāvs Vasks', written over a horizontal line.

Klāvs Vasks
Chairman of the Council

Rīga,
16 May 2011

	Notes	LVL 000's	
		2010 Group	2010 Bank
Interest income	4	25,695	22,379
Interest expense	4	<u>(26,366)</u>	<u>(24,852)</u>
Net interest expense		(671)	(2,473)
Commission and fee income	5	11,201	8,290
Commission and fee expense	5	<u>(3,422)</u>	<u>(2,898)</u>
Net commission and fee income		7,779	5,392
Gain on transactions with financial instruments, net	6	2,504	1,770
Other income	7	3,754	2,742
Other expense		<u>(2,227)</u>	<u>(2,153)</u>
Administrative expense	8,9	(18,016)	(13,398)
Amortisation and depreciation charge	19,20	<u>(3,299)</u>	<u>(1,167)</u>
Impairment charges and reversals, net	10	(9,973)	(10,712)
Gain on disposal of assets held for sale, net		857	-
Loss before taxation		<u>(19,292)</u>	<u>(19,999)</u>
Corporate income tax	11	481	572
Net loss for the period		<u>(18,811)</u>	<u>(19,427)</u>
Attributable to:			
Equity holders of the Bank		(18,811)	(19,427)
Minority interest		<u>-</u>	<u>-</u>
		<u>(18,811)</u>	<u>(19,427)</u>

The notes on pages 13 to 68 are an integral part of these financial statements.

	LVL 000's	
	2010 Group	2010 Bank
Net loss for the period	<u>(18,811)</u>	<u>(19,427)</u>
Other comprehensive income:		
<i>Fair value revaluation reserve: held-to-maturity securities</i>		
Amortisation	363	357
Deferred income tax charged directly to equity	(38)	(35)
<i>Fair value revaluation reserve: available-for-sale securities</i>		
Impairment of securities	357	357
Fair value revaluation reserve charged to statement of income	493	595
Change in fair value of available for sale securities	3,472	3,247
Deferred income tax charged directly to equity	(78)	(51)
<i>Other reserves</i>		
Foreign exchange revaluation reserve	678	-
Other comprehensive income for the period	<u>5,247</u>	<u>4,470</u>
Total comprehensive loss for the period	<u>(13,564)</u>	<u>(14,957)</u>
Attributable to:		
Equity holders of the Bank	(13,564)	(14,957)
Minority interest	-	-
	<u>(13,564)</u>	<u>(14,957)</u>

The notes on pages 13 to 68 are an integral part of these financial statements.

	Notes	LVL 000's	
		31/12/2010 Group	31/12/2010 Bank
<u>Assets</u>			
Cash and deposits with central banks	12	187,220	177,348
Balances due from credit institutions	13	219,624	211,608
Securities held for trading:			
- fixed income	16	140	4
- shares and other non-fixed income	17	34	-
Derivative financial instruments	29	2,670	2,716
Financial assets designated at fair value through profit and loss		3,318	-
Available-for-sale securities:			
- fixed income	16	187,524	143,498
- shares and other non-fixed income	17	9,467	9,429
Loans and receivables to customers	14,15	794,329	691,098
Held-to-maturity securities	16	127,572	117,280
Current income tax assets	11	195	-
Non-current assets and disposal groups classified as held for sale	21	3,289	-
Fixed assets	20	38,072	3,910
Goodwill and intangible assets	19	2,060	1,256
Investments in subsidiaries	18	-	43,839
Investment property		904	-
Deferred income tax assets	11	30,100	29,980
Other assets	22	5,991	3,936
Total assets		<u>1,612,509</u>	<u>1,435,902</u>
<u>Liabilities</u>			
Derivative financial instruments	29	644	702
Financial liabilities designated at fair value through profit and loss		1,484	-
Financial liabilities measured at amortised cost:			
- balances due to credit institutions and central banks	24	70,559	82,175
- deposits from customers	25	1,294,335	1,117,274
- issued debt securities	23	91,485	91,557
- other financial liabilities		7,333	-
Current income tax liabilities	11	188	-
Deferred income tax liabilities	11	491	-
Other liabilities	26	12,728	8,919
Subordinated liabilities	27	51,235	51,235
Total liabilities		<u>1,530,482</u>	<u>1,351,862</u>
<u>Equity</u>			
Paid-in share capital	28	103,000	103,000
Reserves		(2,162)	467
Accumulated losses		(18,811)	(19,427)
Total shareholders' equity attributable to the shareholders of the Bank		<u>82,027</u>	<u>84,040</u>
Minority interest		-	-
Total equity		<u>82,027</u>	<u>84,040</u>
Total liabilities and equity		<u>1,612,509</u>	<u>1,435,902</u>

The notes on pages 13 to 68 are an integral part of these financial statements.

Changes in the Group's equity are as follows:

	LVL 000's						
	Attributable to equity holders of the Bank						
	Issued share capital	Fair value revaluation reserve, attributable to:		Foreign exchange reserve	Restructuring reserve*	Accumulated losses	Total equity
	Held-to-maturity securities	Available-for-sale securities					
Balance as at 30 June 2010	4,000	-	-	-	-	-	4,000
Issue of new shares	99,000	-	-	-	-	-	99,000
Restructuring (Note 2)	-	(2,031)	(1,985)	168	(3,561)	-	(7,409)
Net loss for the period	-	-	-	-	-	(18,811)	(18,811)
Other comprehensive income for the period	-	325	4,244	678	-	-	5,247
Balance as at 31 December 2010	103,000	(1,706)	2,259	846	(3,561)	(18,811)	82,027

* When determining the assets and liabilities that were eligible for the transfer of undertaking that took place on 1 August 2010, the composition of assets and liabilities were determined on the parent bank's, i.e. AS Parex Banka stand-alone accounts basis. Any differences in the value of investments in subsidiaries that were transferred to AS Citadele Banka and their net equity as at the date of the transfer, are treated as restructuring reserves in the consolidated financial statements of AS Citadele Banka.

Changes in the Bank's equity are as follows:

	LVL 000's				
	Attributable to equity holders of the Bank				
	Issued share capital	Fair value revaluation reserve, attributable to:		Accumulated losses	Total equity
	Held-to-maturity securities	Available-for-sale securities			
Balance as at 30 June 2010	4,000	-	-	-	4,000
Issue of new shares	99,000	-	-	-	99,000
Restructuring (Note 2)	-	(2,031)	(1,972)	-	(4,003)
Net loss for the period	-	-	-	(19,427)	(19,427)
Other comprehensive income for the period	-	322	4,148	-	4,470
Balance as at 31 December 2010	103,000	(1,709)	2,176	(19,427)	84,040

The notes on pages 13 to 68 are an integral part of these financial statements.

	Notes	LVL 000's	
		2010 Group	2010 Bank
Cash flows from operating activities			
Loss before tax		(19,292)	(19,999)
Amortisation of intangible assets, depreciation of fixed assets and investment property		3,299	1,167
Change in impairment allowances and other provisions		21,165	21,904
Other non-cash items		939	3,739
Cash generated before changes in assets and liabilities		6,111	6,811
Change in derivative financial instruments		(1,638)	(1,576)
(Increase)/ decrease in other assets		600	(1,034)
Increase in other liabilities		3,917	2,979
(Increase)/ decrease in trading investments		(73)	1
(Increase)/ decrease in balances due from credit institutions		(12,587)	4,640
(Increase) / decrease in loans and receivables to customers		61,606	51,026
Increase / (decrease) in balances due to credit institutions and central banks		(25,601)	(28,276)
Increase in deposits from customers		60,270	52,216
Cash generated from operating activities before corporate income tax		92,605	86,787
Corporate income tax		(8)	-
Net cash flow generated from operating activities		92,597	86,787
Cash flows from investing activities			
(Purchase) of intangible and fixed assets		(930)	(520)
Proceeds from disposal of intangible and fixed assets		76	41
(Purchase) of held-to-maturity securities, net		(229)	-
(Purchase) of available-for-sale securities		(74,290)	(57,122)
Cash inflows from available-for-sale securities		23,610	13,034
Increase in cash and cash equivalents as a result of restructuring		206,217	186,977
Increase in cash and cash equivalents as a result of subsidiary acquisition		6,313	-
Net cash flow from investing activities		160,767	142,410
Cash flows from financing activities			
Repurchase of debt securities		(22,347)	(22,347)
Issue of new shares		99,000	99,000
Net cash flow from financing activities		76,653	76,653
Net cash flow for the period		330,017	305,850
Cash and cash equivalents at the beginning of the period		4,000	4,000
Cash and cash equivalents at the end of the period	32	334,017	309,850

The Group as a result of subsidiary acquisition received LVL 155 million of loans and receivables, LVL 27 million of other assets that are not cash or cash equivalents, LVL 123 million of customer deposits and LVL 34 million of other liabilities that are not cash or cash equivalents.

Amounts of interest income and (expense) received/ (paid) are as follows:

	LVL 000's	
	2010 Group	2010 Bank
Interest income received during the period	24,923	21,695
Interest expense paid during the period	(26,168)	(24,382)

The notes on pages 13 to 68 are an integral part of these financial statements.

If not mentioned otherwise, referral to Group's policies and procedures should be also considered as referral to the respective Bank's policies and procedures.

AUTHORISATION OF THE FINANCIAL STATEMENTS

These financial statements have been authorised for issuance by the Management on 16 May 2011. In accordance with the Commercial Law of the Republic of Latvia, the shareholders' meeting has the right to make the decision on the approval of the financial statements.

NOTE 1. GENERAL INFORMATION

AS Citadele Banka (hereinafter – the Bank) was registered as a joint stock company on 30 June 2010. The Bank commenced its operations on 1 August 2010.

The Bank's head office is located in Riga, Latvia. The legal address of the Bank is Republikas laukums 2a, Riga, LV-1010. As at 31 December 2010, the Bank was operating a total of 44 branches and client service centres in Riga and throughout Latvia. The Bank has 7 foreign branches and client service centres – in Tallinn (Estonia), Narva (Estonia), Hamburg (Germany), Munich (Germany), Stockholm (Sweden) and Goteborg (Sweden). The Bank owns directly and indirectly 19 subsidiaries, which operate in various financial markets sectors. The Bank is the parent company of the Group.

The Group's main areas of operation include accepting deposits from customers, granting short-term and long-term loans to a wide range of customers and servicing payment cards, dealing with finance lease and foreign exchange transactions. The Bank offers its clients also trust management and private banking services, performs local and international payments, as well as provides a wide range of other financial services.

As at 31 December 2010, the Group had 1,762 full time employees and the Bank had 1,329 full time employees.

NOTE 2. RESTRUCTURING

On 30 June 2010 AS Citadele Banka was registered in the commercial registry of the Republic of Latvia and on the same date it received banking licence from the Financial and Capital Market Commission (FCMC). AS Citadele Banka was established as a result of implementation of AS Parex Banka's restructuring plan, which was approved by the Cabinet of Ministers in the spring of 2010 and pursuant to which AS Citadele Banka was to take over from AS Parex Banka certain assets and liabilities and other items, i.e. an undertaking.

The transfer of undertaking from AS Parex Banka to AS Citadele Banka took place on 1 August 2010. The transfer of undertaking was performed under Article 59.2 of the Latvian Law on Credit Institutions (further also – CIL). Legal definition of undertaking is given in the same Article 59.2 of CIL. Transfer of undertaking is a civil law transaction between two parties: the transferor, AS Parex Banka, and the transferee, AS Citadele Banka, whereby the transferee acquires title to the transferred undertaking. The transferred undertaking, i.e. the components thereof, is agreed by both banks and defined in the agreement on transfer of undertaking, which was entered into on 28 July 2010.

The steps, which according to law need to be taken in order to execute transfer of undertaking of a credit institution differ from those needed to be taken when doing general reorganisation. The reason for that is that the transfer of credit institution's undertaking is not a type of general reorganisation of a credit institution and different provisions of legal enactments have to be applied and complied with when doing one or the other. One of the most distinct differences and features is the fact that a credit institution is entitled not to seek consent of any creditor or other party in order to transfer its undertaking. The only permission/approval, which needs to be received, is from Financial and Capital Markets Commission as stipulated by Article 59.2 of CIL.

The steps and legal documentation in regard to the transfer of undertaking, i.e. restructuring, were as follows:

- (a) The credit institution (according to its corporate procedures) takes a decision to implement a transfer of undertaking (i.e. a transfer of property and/or assets and/or liabilities);

On 28 July 2010 the Management Boards of AS Parex Banka and AS Citadele Banka passed the decisions, whereby both banks decided to enter into an agreement on transfer of undertaking from AS Parex Banka to AS Citadele Banka. Approvals from supervisory board of each bank were received also on the same date. AS Parex Banka in addition to entering into the agreement on transfer of undertaking decided to submit to the FCMC proposal for transfer of undertaking in accordance with the agreement on transfer of undertaking.

- (b) An agreement regarding the transfer, and any other required document depending on the exact content of undertaking, to be transferred, are drafted;

The business transfer agreement (In Latvian: Līgums par uzņēmuma pāreju) was signed by and between both banks on 28 July 2010.

- (c) A proposal for the transfer of undertaking, together with an evaluation of the ordinary value, in the conditions of a functioning market, of the assets and liabilities included in the undertaking, made by an eligible expert no more than 30 days before the proposal, is submitted to the FCMC;

On 28 July 2010 AS Parex Banka submitted to FCMC proposal for transfer of undertaking together with a copy of the signed business transfer agreement and an evaluation of the ordinary value, in the conditions of a functioning market, of the assets and liabilities included in the undertaking, made by SIA KPMG Baltics and dated 26 July 2010.

- (d) The FCMC, upon a review of proposal and the evaluation, and any other facts and information it considers relevant, takes a decision either permitting the transfer of undertaking or not permitting it;

On 30 July 2010 FCMC, namely its council, passed a decision No.213 to permit the transfer of undertaking to occur.

- (e) If the FCMC has decided to permit the transfer of undertaking, the credit institution and the transferee concerned can proceed with the transfer;

On 30 July 2010 after receipt of the above referred FCMC decision both banks signed a certificate acknowledging that all conditions precedent set forth in the business transfer agreement in order for the transfer to take place on 1 August 2010 did occur and that the transfer is to be done. On 1 August 2010 transfer of undertaking took place in accordance with the concluded agreement.

- (f) In the course of the transfer, or once the relevant asset or liability has been transferred to the transferee, the transferee (and, if needed, the transferor) notify the relevant counterparties thereof so that the contractual relationships can continue without disturbance;

AS Citadele Banka started to send out notifications to clients on 1 August 2010.

- (g) Any applicable public registration or similar procedures need to be implemented (for example, in respect of particular types of assets), either during the transfer or afterwards, as appropriate;

Registrations in public registries in order to perfect the transfer of undertaking have been taking place since 1 August 2010 and according to plan should have been gradually finished by the end of 2010. At the date of signing these financial statements, some registration procedures still continue. However, the management of the Bank strongly believe that any outstanding procedures will not impact the Bank's ability to continue servicing the clients.

- (h) Any applicable consents from governmental authorities that are needed under the relevant applicable laws must also be obtained as required by those laws;

Consents, where necessary, have been obtained. In order to thoroughly identify the necessary consents and approvals and to receive them as required, the bank received legal opinions and legal assistance from reputable lawyers in each of the jurisdictions of its operations and assets.

Process of perfection of title over the transferred undertaking has been taking place ever since 1 August 2010 and is expected to be finalised during the first half of 2011. For the purposes of perfection not only Latvian law is applicable, but also law of each jurisdiction which is applicable to the component of undertaking in question.

Restructuring implications

The Bank's establishment and future operations are part of the restructuring plan of AS Parex Banka that was approved by European Commission (further EC). On 15 September 2010, EC adopted the decision *On the State Aid C 26/2009 (ex N 289/2009)* that the restructuring aid which Latvia implements for AS Parex Banka and AS Citadele Banka is found to be compatible with the internal market within the meaning of Article 107(3)(b) of the Treaty on the Functioning of the European Union. To comply with the aforementioned requirements, the Bank has undertaken certain commitments in relation to the future business operations. The commitments have been taken into account, when preparing the long-term business plan of the Bank. During 2010, the Bank has complied with the commitments.

Impact of financial crisis on the Group and Bank

The collapse of Lehman Brothers in mid-September 2008 and the unprecedented events in subsequent weeks intensified the turmoil in global financial markets leading to increased public uncertainty. Even though in 2010 global and Latvian economy experienced an economic upturn, there still remains uncertainty about the economic development in the future.

Borrowers of the Group and liquidity of certain types of assets may be affected by the financial crisis. This has been properly reflected by the management of the Bank in its estimates of expected future cash flows in asset impairment assessments.

NOTE 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Certain new standards and interpretations have been published that are mandatory for the Group's accounting periods beginning on or after 1 January 2011 or later periods and which the Group has early adopted:

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. As a result the Bank and Group does not disclose transactions with government – related entities that are part of the Group's normal business.

Certain new standards and interpretations have been published that become effective for the accounting periods beginning on or after 1 January 2010 or later periods and which are not relevant to the Group or are not yet endorsed by the EU:

- Classification of Rights Issues - Amendment to IAS 32 (issued 8 October 2009; effective for annual periods beginning on or after 1 February 2010).
- IFRS 9, Financial Instruments Part 1: Classification and Measurement (not yet endorsed by the EU).
- IFRS 9 adoption is required starting 1 January 2013, yet earlier application is also allowed, not yet endorsed by the EU.
- IFRIC 19, Extinguishing financial liabilities with equity instruments (effective for annual periods beginning on or after 1 July 2010).
- Prepayments of a Minimum Funding Requirement – Amendment to IFRIC 14 (effective for annual periods beginning on or after 1 January 2011).
- 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).
- 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 have not yet been adopted by the EU).
- Disclosures—Transfers of Financial Assets – Amendments to IFRS 7 (effective for annual periods beginning on or after 1 July 2011; not yet adopted by the EU)
- Deferred Tax: Recovery of Underlying Assets – Amendment to IAS 12 (effective for annual periods beginning on or after 1 January 2012; not yet adopted by the EU).
- 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; not yet adopted by the EU).

The Group is in the process of evaluating the potential effect if any of these new standards and interpretations.

a) Basis of preparation

These financial statements are prepared in accordance with International Financial Reporting Standards (IFRS) as adopted in the European Union on a going concern basis. The financial statements are prepared under the historical cost convention, except for available-for-sale financial assets, financial assets and financial liabilities held at fair value through profit or loss, trading securities and all derivative contracts, which have been measured at fair value.

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.

b) Functional and Presentation Currency

The functional currency of each of the Group's consolidated entities is the currency of the primary economic environment in which the entity operates. The functional currency of the Bank and its Latvian subsidiaries, and the Group's presentation currency, is the national currency of the Republic of Latvia, Latvian lats ("LVL"). The accompanying financial statements are presented in thousands of Lats (LVL 000's).

c) Accounting for restructuring/ transfer of undertaking

When determining the assets and liabilities that were eligible for the transfer of undertaking that took place at the beginning of 1 August 2010, the composition of assets and the liabilities were determined on the parent bank's, i.e. AS Parex Banka stand-alone accounts basis. Any differences in the carrying value of investments in subsidiaries that were transferred to AS Citadele Banka and their net equity as at the date of transfer, are treated as restructuring reserves in the consolidated financial statements of AS Citadele Banka. Group's financial statements incorporate the transferred subsidiaries' results only from the date on which the restructuring between entities under common control occurred, i.e. 1 August 2010.

The carrying amount of net assets that were transferred to the Bank equalled zero. Since the carrying value of net assets was zero and any possible impairment could not reduce the value of net assets below zero, the fair value less costs to sell of the net assets transferred to the Bank equalled the carrying amount of those net assets. The transfer transaction was accounted using predecessor accounting i.e. the transferred assets and liabilities were initially recognised at their carrying amount as in the predecessor bank.

d) Basis of Consolidation

As at 31 December 2010, the Bank had a number of investments in subsidiaries, in which the Bank held directly and indirectly more than 50% of the shares and voting rights, and accordingly, had the ability to exercise control. The investments in the subsidiaries are presented in the Bank's financial statements at acquisition cost. More detailed information on the Group's subsidiaries is presented in Note 18.

The financial statements of AS Citadele Banka and its subsidiaries are consolidated in the Group's financial statements on a line by line basis by adding together like items of assets and liabilities as well as income and expenses. For the purposes of consolidation, intra-group balances and intra-group transactions, including interest income and expense as well as unrealised profits and loss resulting from intra-group transactions, are eliminated in the Group's financial statements. However, intra-group losses may indicate an impairment that requires recognition in the Group's financial statements.

e) Income and Expense Recognition

Interest income and expense items are recognised on an accrual basis using the effective interest rate.

Commissions in respect of the acquisition of financial assets or the issue of financial liabilities that are not at fair value through profit or loss are deferred and recognised as an adjustment to the effective yield on the respective asset or liability. Other commissions and fees are credited and/ or charged to the statement of income as services are provided or on the execution of a significant act, as applicable, under the line "commission and fee income" or "commission and fee expense", as appropriate.

Penalty income is recognised on cash-received basis.

f) Foreign Currency Translation

Transactions denominated in foreign currencies are recorded in Lats at actual rates of exchange effective at the date of the transaction. Non-monetary items that are measured at fair value in a foreign currency, such as investments in equity instruments, are translated using the exchange rates at the date, when the fair value was determined and the impact from changes in foreign exchange rates are treated as foreign exchange gain/loss in the income statement. Monetary assets and liabilities denominated in foreign currencies are translated into Lats at the official rate of exchange prevailing at the end of the year. 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 income as a profit or loss from revaluation of foreign currency positions.

The results and financial position of all the Group's entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each statement of financial position presented are translated at the closing rate at the date of that statement of financial position;
- income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions).
- all resulting exchange differences are recognised as other comprehensive income.

g) Taxation

For the year period 31 December 2010 corporate income tax is applied at the rate of 15% on taxable income generated by the Bank for the taxation period.

Deferred income tax is provided using the balance sheet liability method for tax loss carry forwards and temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit. Deferred tax liabilities are not recorded for temporary differences on initial recognition of goodwill and subsequently for goodwill which is not deductible for tax purposes. Deferred tax balances are measured at tax rates enacted or substantively enacted at the end of the reporting period which are expected to apply to the period when the temporary differences will reverse or the tax loss carry forwards will be utilised. Deferred tax assets and liabilities are netted only within the individual

companies of the Group. Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilised.

The carrying amount of deferred corporate income tax asset, if any, is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised. The future taxable profits and the amount of tax benefits that are probable in the future are based on a medium term financial forecast prepared by management and extrapolated results thereafter. The financial forecast is based on management expectations that are believed to be reasonable under the circumstances.

h) Financial instruments

The Group recognises financial asset on its balance sheet when, and only when, the Group becomes a party to the contractual provisions of the instrument.

Financial assets in the scope of IAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, or available-for-sale financial assets, as appropriate. At initial recognition, the financial assets are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable incremental transaction costs. The classification of investments between the categories is determined at acquisition based on the guidelines established by the Management.

All "regular way" purchases and sales of investments are recognised using settlement date accounting. The settlement date is the date when an asset is delivered to or by the Group. Settlement date accounting refers to the recognition of an asset on the day it is transferred to the Group and to the derecognition of an asset, on the day that it is transferred by the Group.

Financial assets and liabilities held for trading

Financial assets and liabilities classified as held for trading are included in the category "financial assets/ liabilities at fair value through profit or loss". Financial assets and/ or liabilities are classified as held for trading if they are either acquired for generating a profit from short-term fluctuations in price or dealer's margin, or are included in a portfolio in which a pattern of short-term profit taking exists. Held for trading financial assets and liabilities are subsequently re-measured at fair value based on available market prices or quotes of brokers. The result of re-measuring trading financial assets and liabilities at fair value is charged directly to the statement of income.

Financial assets/ liabilities designated at fair value through profit and loss

Included in this category are (a) unit-linked investment contract liabilities and respective investments and (b) certain securities, which are managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy. According to unit-linked investment contract term, the credit risk associated with the investments made by the insurance underwriter is fully attributable to the counterparty entering the insurance agreement and not the underwriter. As such, by designating both assets acquired and liabilities undertaken at fair value through profit and loss, potential accounting mismatch is avoided.

Excluding interest on interest rate swaps, interest on financial assets at fair value through profit or loss held on own account is included in net interest income. Revaluation and trading gains and losses arising from changes in fair value of the respective assets, as well as interest on interest rate swaps are included directly in the income statement's line "(Loss)/gain on transactions with financial instruments, net".

Held to maturity investments

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held to maturity if the Group has both the positive intent and ability to hold these investments to maturity. Held-to-maturity financial assets are carried at amortised cost using the effective interest rate method, less any allowance for impairment.

A financial asset is impaired if its carrying amount is greater than its estimated recoverable amount. The amount of the impairment loss for assets carried at amortised cost is calculated as the difference between the asset's carrying amount and the present value of expected future cash flows discounted at the financial instrument's original effective interest rate.

When available-for-sale assets are reclassified to held-to-maturity category, the fair value of the reclassified available-for-sale asset as at the date of reclassification further becomes the amortised cost. The fair value as of the date of reclassification is the deemed cost of the reclassified assets. The fair value revaluation reserve attributable to reclassified assets are amortised until the asset's maturity using effective interest rate method. If there is objective evidence that the value of reclassified assets has been impaired, the unamortised negative fair value revaluation reserve that has been recognised directly in equity is charged to the statement of income.

Available for sale financial assets

Available for sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the three preceding categories. The Group's available for sale financial assets are intended to be held for an undefined period of time and may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

Available for sale financial assets are subsequently re-measured at fair value based on available market prices or quotes of brokers. The result of fair value revaluation of available for sale securities is recognised in other comprehensive income statement. The difference between the initial carrying amount and amortised cost determined by the effective interest rate method is treated as interest income. Dividends on available-for-sale equity instruments are recognised in the income statement. When the securities are disposed of, the related accumulated fair value revaluation is included in the statement of income as profit/ (loss) from sale of securities available for sale.

If an available-for-sale financial asset is determined to be impaired, the cumulative gain or loss previously recognised in the statement of comprehensive income is recognised in the income statement. However, interest is calculated using the effective interest method, and foreign currency gains and losses on monetary assets classified as available for sale are recognised in the consolidated income statement.

In the case of equity investments classified as available for sale, a significant or prolonged decline in the fair value of the security below its cost is objective evidence of impairment resulting in the recognition of an impairment loss. If any such evidence exists for available-for sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the income statement.

Derivative Financial Instruments

In the ordinary course of business, the Group engages as a party to contracts for forward foreign exchange rate, currency and interest rate swap instruments and other derivative financial instruments. All derivatives are classified as held-for-trading.

Subsequent to initial recognition, outstanding forward foreign exchange rate contracts, currency swaps and other derivative financial instruments are carried in the balance sheet at their fair value. The fair value of these instruments is recognised on the balance sheet under designated assets and liabilities caption "Derivative financial instruments".

Gains or losses from changes in the fair value of outstanding forward foreign exchange rate contracts, currency and interest rate swaps and other derivative financial instruments are recognised in the statement of income as they arise.

Own credit risk in valuations of derivative liabilities

The Group's own credit changes are reflected in valuations of such derivative liabilities, where the Group's own credit risk would be considered by market participants and excludes derivatives for which it is established market practice not to include an entity-specific adjustment for own credit, also referred to as counterparty close out approach. This amount represents the estimated difference in the market value of identical obligations issued by a riskless intermediary, relative to the market value of those obligations issued by the Group, as judged from the perspective of the holders of those obligations. Own credit changes were calculated based on credit default swap spreads. At 31 December 2010, there are no material liabilities / assets arising from Group's own credit assessment.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are carried at amortised cost using the effective interest method. Gains and losses are recognised in income when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Loans and receivables are recognised on drawdown. From the date of signing a contractual agreement till drawdown they are accounted for as loan commitments off balance sheet.

When the loans or receivables cannot be recovered, they are written-off and charged against impairment for credit losses. The management of the Group makes the decision on writing-off loans. Recoveries of loans previously written-off are credited to the statement of income.

Included in the category of "loans and receivables" are such financial instruments: a) cash and deposits with central banks, b) balances due from credit institutions and c) loans and receivables to customers.

Issued debt, subordinated debt and other borrowed funds

The Group recognises financial liabilities on its balance on drawdown.

After initial measurement, being fair value plus directly attributable transaction costs, debt issued, subordinated debt and borrowings are measured at amortised cost and any difference between net proceeds and value at redemption is recognised in the statement of income over the period of borrowings using the effective interest rate.

i) Sale and Repurchase Agreements

These agreements are accounted for as financing transactions. Under sale and repurchase agreements, where the Group is the transferor, assets transferred remain on the Group's balance sheet and are subject to the Group's usual accounting policies, with the purchase price received included as a liability owed to the transferee. Assets in the balance sheet are shown separately from other assets when the transferee has the right by contract or custom to sell or repledge the collateral.

Where the Group is the transferee, the assets are not included in the Group'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 income over the term of the agreement.

j) Derecognition of Financial Assets and Liabilities

Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- the rights to receive cash flows from the asset have expired; or
- the Group has transferred its rights to receive cash flows from the asset, or retained the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass-through' arrangement; and
- the Group either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Where continuing involvement takes the form of a written and/ or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Group's continuing involvement is the amount of the transferred asset that the Group may repurchase, except that in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, the extent of the Group's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

Collateral (shares and bonds) furnished by the Group under standard repurchase agreements and securities lending and borrowing transactions is not derecognised because the Group retains substantially all the risks and rewards on the basis of the predetermined repurchase price, and the criteria for derecognition are therefore not met.

Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in profit or loss.

k) Leases

Finance leases – Group as lessor

Finance leases, which transfer substantially all the risks and rewards incidental to ownership of the assets, are recognised as assets at amounts equal at the inception of the lease to the net investment in the lease. The finance income is allocated to periods during the lease term to produce a constant periodic return on the net investments outstanding in respect of the finance leases.

For the purposes of these financial statements, finance lease receivables are included in loans and receivables to customers.

Operating leases – Group as lessor

The Group presents assets subject to operating leases in the balance sheets according to the nature of the asset. Lease income from operating leases is recognized in statement of income on a straight-line basis over the lease term as other income. The aggregate cost of incentives provided to lessees is recognized as a reduction of rental income over the lease term on a straight-line basis. Initial direct costs incurred specifically to earn revenues from an operating lease are added to the carrying amount of the leased asset.

The depreciation policy for depreciable leased assets is consistent with the lessor's normal depreciation policy for similar assets, and depreciation is calculated in accordance with accounting policies, used for the Group's property, plant and equipment.

Operating leases – Group as lessee

Leases of assets under which substantially all the risks and rewards of ownership are retained by the lessor are classified as operating leases. Lease payments under an operating lease are recognized as expenses on a straight-line basis over the lease term and included into administrative expenses.

l) Impairment of loans and receivables to customers

The Group has granted commercial and consumer loans to customers throughout its market area. The economic conditions of the market the Group operates in may have an impact on the borrowers' ability to repay their debts. The Management of the Group have considered both specific and portfolio-level risks in determining the balance of impairment allowance for incurred credit losses.

The Management of the Group assess at each balance sheet date whether there is objective evidence that a loan or portfolio of loans and receivables to customers is impaired. A loan or portfolio of loans and receivables to customers is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more loss events that occurred after the initial recognition of the loan and that loss event (or events) has had an impact such that the estimated present value of future cash flows is less than the current carrying value of the loan or portfolio of loans and receivables to customers, and can be reliably estimated.

Objective evidence that a loan or portfolio of loans and receivables to customers is potentially impaired includes the following observable data that comes to the attention of the Group:

- significant financial difficulty of the borrower;
- a breach of contract, such as a default or delinquency in interest or principal payments;
- the granting to the borrower of a concession, for economic or legal reasons relating to the borrower's financial difficulty, that the Group would not otherwise consider;
- it becoming probable that the insolvency process may be initiated against the borrower, or the borrower will enter other financial reorganisation;
- the worsening of economic conditions in the market segment, where the borrower operates; or
- observable data indicating the there is a measurable decrease in the estimated future cash flows from a portfolio of loans and receivables to customers since the initial recognition of those of loans and receivables, although the decrease cannot yet be identified with the individual loans in the portfolio, including:
 - adverse changes in the payment status of borrowers in the portfolio; or
 - national or local economic conditions that correlate with defaults on the loans and receivables in the portfolio.

The Group first assesses whether objective evidence of impairment exists individually for loans and receivables that are individually significant, and individually or collectively for loans and receivables that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed loan, whether significant or not, it includes that loan in a group of loans and receivables with similar credit risk characteristics and collectively assesses them for impairment. Collectively assessed impairment losses represent an

interim step pending the identification of impairment losses on individual loans in a group of loans and receivables. As soon as information is available that specifically identifies losses on individually impaired loans in a group, those loans are removed from the group. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

For loans and receivables, the amount of impairment loss is measured as the difference between the loan's carrying amount and the present value of estimated future cash flows discounted at the loan's original effective interest rate. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. The calculation of the present value of the estimated future cash flows of a collateralised loan reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable. The amount of the loss is recognised in the statement of income.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was initially recognised, the previously recognised impairment loss is reversed. Any subsequent reversal of the impairment loss is recognised in the statement of income, to the extent that the carrying value of the loan does not exceed what its amortised cost would have been absent the impairment at the reversal date.

When a borrower fails to make a contractually due payment of interest or principal, but the Group believes that impairment is not appropriate on the basis of the level of security/ collateral available and/ or the stage of collections of amounts owed to the Group, the carrying amount of the loan is classified as past due but not impaired.

When loans and receivables cannot be recovered, they are written off and charged against impairment allowance. They are not written off until the necessary legal procedures have been completed and the amount of the loss is finally determined. Subsequent recoveries of amounts previously written off are reported in the statement of income as other operating income.

m) Impairment of available-for-sale and held-to-maturity securities

Evidence of impairment is assessed by reference to the most up to date market valuations, market depth of the respective security, past trading performance and all other available information. The determination of whether or not objective evidence of impairment is present requires the exercise of management judgement. If the Group does not have market valuations, the evidence of impairment is assessed based on credit risk triggers (event of insolvency, any delay of payments, restructuring of debt) and individual credit risk analysis of the issuer.

n) Business combinations and goodwill

Business combinations are accounted for using the purchase method of accounting, which, in essence, involves recognizing identifiable assets, liabilities and contingent liabilities of the acquired business at fair value. Any excess of the cost of acquisition over the fair value of identifiable net assets acquired is recognized as goodwill. If the cost of acquisition is less than fair value of the identifiable net assets acquired, the discount on acquisition is recognized in the income statement in the year of acquisition.

Following the initial recognition, in Group accounts the goodwill arising from the business combinations is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment at each reporting date, or more frequently if events or changes in circumstances indicate that the carrying amount of the goodwill may be impaired.

o) Intangible Assets

Intangible assets comprise software. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition. Subsequent the initial recognition, intangible assets are carried at cost less accumulated amortisation and any accumulated impairment loss.

Leasehold rights are amortised over the remaining lease contract on a straight-line basis. Annual amortisation rates applied on a straight-line basis to software and other intangible assets range from 7% to 50%. All intangible assets, except for goodwill, are with definite lives.

p) Fixed Assets

Fixed assets are recorded at historical cost less accumulated depreciation less any impairment losses. Fixed assets are periodically reviewed for impairment. If the recoverable value of a fixed asset is lower than its carrying amount, the respective asset is written down to its recoverable amount.

Depreciation is calculated using the straight-line method based on the estimated useful life of the asset. The following depreciation rates have been applied:

Category	Annual depreciation rate
Buildings	2%
Transport vehicles	20%
Other fixed assets	20% - 33%

Leasehold improvements are capitalised and depreciated over the remaining lease contract period on a straight-line basis. Land and assets under construction are not depreciated.

Certain reconstruction and renovation costs of buildings, which improve their quality and performance, are capitalised and amortised over the estimated useful life on a straight-line basis.

Maintenance and repair costs are charged to the statement of income as incurred.

q) Assets held for sale

The Group from time to time repossesses from its customers certain assets serving as collateral, when the customer cannot otherwise meet his payment obligations and other loan work-out measures have been unsuccessful. Such assets are classified as held for sale, because they are acquired primarily for the purpose of selling them in the near term. Assets classified as held for sale are stated at the lower of their carrying amount of the outstanding debt and fair value less costs to sell of the tangible asset. At least at each reporting date, the Group assesses, whether the value of the repossessed assets is impaired. The impairment loss reduces carrying amount of the asset and is included in the income statement's line "Impairment charges and reversals, net".

r) Provisions

Provisions are recognised when the Group 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.

s) Off-balance Sheet Financial Commitments and Contingent Liabilities

In the ordinary course of business, the Group is involved with off-balance sheet financial commitments and contingent liabilities comprising commitments to extend loans and receivables to customers, commitments for unutilised credit lines or credit card limits, financial guarantees and commercial letters of credit.

Such financial instruments are recorded in the financial statements as follows:

- commitment to extend loans and advances, credit card and overdraft facilities are recognized on drawdown; and
- financial guarantees and letters of credit are recognized when the related fee received as consideration is recognized.

Commitments to extend loans and receivables and commitments for unutilised credit lines or credit card limits represent contractual commitments to make loans and revolving credits. Commitments generally have fixed expiration dates, or other termination clauses. Since commitments may expire without being drawn upon, the total contract amounts do not necessarily represent future cash requirements.

On initial recognition financial guarantee contracts are measured at fair value. Subsequently, they are carried at the higher of the amount initially recognised less cumulative amortisation over the life of the guarantee and the amount determined in accordance with the accounting policy for provisions when enforcement of the guarantee has become probable.

The methodology for provisioning against possible losses arising from off-balance sheet financial commitments and contingent liabilities is consistent with that described in paragraph r).

t) Trust Activities

Funds managed by the Group on behalf of individuals, corporate customers, trusts and other institutions are not regarded as assets of the Group and, therefore, are not separately included in the balance sheet. Funds under trust management are presented in these financial statements only for disclosure purposes.

u) 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 and willing parties in an arm's length transaction. Where available and reasonably reliable, fair values are determined by reference to observable market prices. Where representative market prices are not available or are unreliable, fair values are determined by using valuation techniques which refer to observable market data. These include prices obtained from independent market surveys, comparisons with similar financial instruments, discounted cash flow analyses and other valuation techniques commonly accepted and used by market participants.

Future events may occur which will cause the assumptions used in arriving at the estimates to change. The effect of any changes in estimates will be recorded in the financial statements, when determinable. Further, changes and movement in market conditions may affect accuracy of the fair value calculations so that the actual outcome of the transactions is different from the one reported in the financial statements. Also, when changed, management estimates used in preparing these financial statements could impact the reported result of the Group.

v) Cash and Cash Equivalents

For the purpose of presentation in the statement of cash flows, cash and cash equivalents are defined as the amounts comprising cash and demand deposits with central banks and other credit institutions with an insignificant risk of changes in value and a remaining maturity of not more 3 months from the date of acquisition, less demand deposits due to credit institutions.

w) Offsetting

Financial assets and liabilities are offset and the net amount is reported in the balance sheet when there is a currently enforceable legal right to set off the recognized amounts and there is an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously.

x) Staff costs and related contributions

The Group and the Bank pays social security contributions to state pension insurance and to the state funded pension scheme in accordance with Latvian and relevant foreign regulations. In accordance with the Rules of the Cabinet of Ministers of Latvia circa 65% of the social insurance contributions are used to fund the state defined contribution pension system. State funded pension scheme is a defined contribution plan under which the Group and the Bank pay fixed contributions determined by law and will have no legal or constructive obligation to pay further contributions if the state pension insurance system or state funded pension scheme are not able to settle their liabilities to employees. The social security contributions are accrued in the year in which the associated services are rendered by the employees of the group.

y) Events after the balance sheet date

Post-year-end events that provide additional information about the Bank's position at the balance sheet date (adjusting events) are reflected in the financial statements. Post-year-end events that are not adjusting events are disclosed in the notes if material.

z) Use of estimates in the preparation of financial statements

The preparation of financial statements in conformity with International Financial Reporting Standards as adopted by EU, requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, income and expenses and disclosure of contingencies. The management has applied reasonable and prudent estimates and judgments in preparing these financial statements. The significant areas of estimation used in the preparation of the accompanying financial statements relate to evaluation of impairment for financial assets losses, determining fair values of the financial assets and liabilities and estimating future periods' taxable profit in order to assess amount of deferred tax assets that can be utilised and, as such, recognised.

Impairment of loans

The Group regularly reviews its loans and receivables to assess impairment. The estimation of potential impairment losses is inherently uncertain and dependant upon many factors. On an on-going basis potential issues are identified promptly as a result of individual loans being regularly monitored. Impairment losses are calculated on an individual basis with reference to expected future cash flows including those arising from the realisation of collateral. The Group uses its experienced judgement to estimate the amount of any impairment loss considering matters such as future economic conditions and the resulting trading performance of the borrower and the value of collateral, for which there may not be a readily accessible market. As a result, the impairment losses can be subject to significant variation as time progresses and the circumstances become clearer. 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.

In addition, the Group estimates collective impairment losses to cover losses inherent in the loan portfolio where there is objective evidence to suggest that it contains impaired loans, although the individual impaired loans cannot yet be identified. The collective impairment losses take account of observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans and receivables with similar credit risk characteristics, although the decrease cannot yet be identified with the individual loans in the portfolio.

Future cash flows in a portfolio of loans and receivables that are collectively evaluated for impairment are estimated on the basis of historical loss experience for loans and receivables with credit risk characteristics similar to those in the portfolio. Historical loss experience is adjusted for current observable market data using the Group's experienced judgement 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 future credit quality of the loan portfolio for which the collective impairment losses are estimated is subject to uncertainties that could cause actual credit losses to differ materially from reported impairment losses. These uncertainties include factors such as international and local economic conditions, borrower specific factors, industry and market trends, interest rates, unemployment rates and other external factors. Changes in the Bank's LGD ratio by 500 basis points would result in increase/ decrease in collectively assessed impairment by ca. LVL 1.96 million.

Impairment of securities

The Group makes various estimates to determine the value of securities assessed for impairment. When the value of securities, for which loss event have occurred, is assessed for impairment, an estimate is made involving factors such as liquidity (quoted prices and volumes from several reliable providers as well as judgemental evaluation), spreads (estimation of securities' spreads and spreads on securities rated Caa1 and below), ratings (subordination) and loss-given-default (LGD) rates.

The future credit quality of the securities for which the impairment losses are estimated is subject to uncertainties that could cause actual credit losses to differ materially from reported impairment losses. These uncertainties include factors such as international, regional and local economic conditions, issuer specific factors, market activity and depth, interest rates and other external factors. As at 31 December 2010, increase or decrease in credit spread delta by 200 basis points would result in no additional impairment for the Bank.

Deferred tax asset

The future taxable profits and the amount of tax benefits that are probable in the future are based on a medium term financial forecast prepared by management and extrapolated results thereafter. The aforementioned forecasts indicate that the Bank will have sufficient taxable profits in the future periods to realise the recognised deferred tax asset.

NOTE 4. INTEREST INCOME AND EXPENSE

	LVL 000's	
	2010 Group	2010 Bank
Interest income:		
- interest on financial assets measured at amortised cost:		
- <i>interest on loans and receivables to customers</i>	21,421	18,799
- <i>interest on balances due from credit institutions and central banks</i>	20,095	17,441
- <i>interest on held-to-maturity securities</i>	512	701
- interest on available-for-sale securities	814	657
- interest on held for trading securities	4,181	3,519
- interest income on financial assets designated at fair value through profit or loss	66	61
	27	-
Total interest income	25,695	22,379
Interest expense:		
- interest on financial liabilities measured at amortised cost:		
- <i>interest on deposits from customers</i>	(26,366)	(24,852)
- <i>interest on subordinated liabilities</i>	(20,075)	(18,454)
- <i>interest on issued debt securities</i>	(3,761)	(3,761)
- <i>interest on balances due to credit institutions and central banks</i>	(2,507)	(2,509)
- <i>interest on other financial liabilities</i>	(14)	(128)
	(9)	-
Total interest expense	(26,366)	(24,852)
Net interest expense	(671)	(2,473)

	LVL 000's	
	2010 Group	2010 Bank
Interest income recognised on impaired assets	5,403	5,698

NOTE 5. COMMISSION AND FEE INCOME AND EXPENSE

	LVL 000's	
	2010 Group	2010 Bank
Commission and fee income:		
- transactions with settlement cards	5,357	4,862
- payment transfer fee	1,955	1,477
- custody, trust and asset management fees	1,729	125
- securities, financial instrument brokerage fees	475	422
- service fee for account maintenance	451	393
- cash disbursement/ transaction commission	436	283
- cash collection	348	348
- letters of credit and guarantees	127	66
- review of loan applications and collateral evaluation	69	64
- other fees	254	250
Total commission and fee income	11,201	8,290

	LVL 000's	
	2010 Group	2010 Bank
Commission and fee expense:		
- fees related to settlement card operations	(2,767)	(2,312)
- fees related to correspondent accounts	(431)	(384)
- brokerage and custodian fees:	(183)	(198)
- securities, financial instrument brokerage fees	(127)	(108)
- custody, trust and asset management fees	(56)	(90)
- other fees	(41)	(4)
Total commission and fee expense	(3,422)	(2,898)
Net commission and fee income	7,779	5,392

Commission and fee income and expense from financial instruments not at fair value through profit and loss, other than amounts included in determining the effective interest rate, can be specified as follows:

	LVL 000's	
	2010 Group	2010 Bank
Commission and fee income	11,201	8,290
Commission and fee expense	(3,422)	(2,898)

NOTE 6. GAIN ON TRANSACTIONS WITH FINANCIAL INSTRUMENTS, NET

	LVL 000's	
	2010 Group	2010 Bank
Gain from trading and revaluation of securities held for trading purposes, net	17	7
Loss from disposal of available for sale securities, net	(493)	(595)
Gain on financial assets measured at amortised cost, net	275	-
Gain from foreign exchange trading and revaluation of open positions, net	3,888	3,346
Loss from trading and revaluation of other derivatives, net	(1,183)	(988)
Gain on trading with financial instruments, net	2,504	1,770

	LVL 000's	
	2010 Group	2010 Bank
Net loss on financial instruments not at fair value through profit or loss	(218)	(595)
Net gain on financial instruments at fair value through profit or loss	2,722	2,365
Total gain on financial instruments, net	2,504	1,770

NOTE 7. OTHER INCOME

	LVL 000's	
	2010 Group	2010 Bank
Penalties received	2,288	1,925
Dividends received	1	1
Other income	1,465	816
Total other operating income	3,754	2,742

NOTE 8. ADMINISTRATIVE EXPENSE

	LVL 000's	
	2010 Group	2010 Bank
Personnel expense	11,556	8,218
Rent, utilities, maintenance	1,522	2,106
IT equipment and software related expense	1,114	663
Non-refundable value added tax	701	495
Consulting and professional fees	572	224
Advertising, marketing and sponsorship	468	366
Office administration expense	322	269
Communications (telephone, telex, etc.)	284	182
Car maintenance	196	184
Business travel expense	179	131
Insurance	143	82
Representation	104	69
Real estate and other taxes	86	1
Security	73	36
Other administrative expense	696	372
Total administrative expense	18,016	13,398

NOTE 9. PERSONNEL EXPENSE

Personnel expense has been presented in these financial statements within administrative expense. Personnel expense includes remuneration for work to the personnel and related social security contributions and bonuses and other short-term benefits costs.

	LVL 000's	
	2010 Group	2010 Bank
Remuneration (incl. bonuses):		
- management	740	229
- other personnel	8,570	6,387
Total remuneration for work	9,310	6,616
Social security contributions:		
- management	154	55
- other personnel	2,092	1,547
Total social security contributions	2,246	1,602
Total personnel expense	11,556	8,218
Number of full time employees at the end of the period	1,762	1,329

NOTE 10. IMPAIRMENT OF ASSETS AND CHANGES IN IMPAIRMENT ALLOWANCES

An analysis of the change in allowances for impairment of loans and receivables is presented as follows:

	LVL 000's	
	2010 Group	2010 Bank
Total allowance for impairment as a result of the restructuring, including:	52,787	53,397
- loans - specifically assessed impairment	37,514	44,651
- loans - collectively assessed impairment	15,273	8,746
Charge:	14,188	12,415
- loans - specifically assessed impairment	13,201	11,632
- loans - collectively assessed impairment	987	783
Release:	(5,284)	(4,582)
- loans - specifically assessed impairment	(2,755)	(2,373)
- loans - collectively assessed impairment	(2,529)	(2,209)
Provision charged to the statement of income, net, including:	8,904	7,833
- loans - specifically assessed impairment	10,446	9,259
- loans - collectively assessed impairment	(1,542)	(1,426)
Change of allowance due to write-offs, net	(1,055)	(756)
Effect of changes in currency exchange rates:	(3)	49
- loans - specifically assessed impairment	-	49
- loans - collectively assessed impairment	(3)	-
Total allowance for impairment at the end of the period, including:	60,633	60,523
- loans - specifically assessed impairment	46,905	53,203
- loans - collectively assessed impairment	13,728	7,320

An analysis of the change in impairment of other assets is presented as follows:

	LVL 000's	
	2010 Group	2010 Bank
Total allowance for impairment as a result of the restructuring, including:	24,247	17,497
- <i>available-for-sale securities</i>	3,013	3,013
- <i>due from credit institutions</i>	540	540
- <i>other non-financial assets</i>	20,694	13,944
Charge:	1,425	2,883
- <i>available-for-sale securities</i>	357	357
- <i>other non-financial assets</i>	1,068	2,526
Release:	(356)	(4)
- <i>other non-financial assets</i>	(356)	(4)
Provision charged to the statement of income, net, including:	1,069	2,879
- <i>available-for-sale securities</i>	357	357
- <i>other financial and non-financial assets</i>	712	2,522
Change of allowance due to write-offs, net:	(1,115)	-
- <i>other non-financial assets</i>	(1,115)	-
Effect of changes in currency exchange rates:	(15)	(5)
- <i>due from credit institutions</i>	(5)	(5)
- <i>other non-financial assets</i>	(10)	-
Total allowance for impairment at the end of the period, including:	24,186	20,371
- <i>available-for-sale securities</i>	3,370	3,370
- <i>due from credit institutions</i>	535	535
- <i>other non-financial assets</i>	20,281	16,466

NOTE 11. TAXATION

Corporate income tax expense comprises the following items:

	LVL 000's	
	2010 Group	2010 Bank
Current corporate income tax	115	-
Deferred income tax	(858)	(840)
Tax withheld abroad	268	268
Prior year adjustments	(6)	-
Total corporate income tax expense	(481)	(572)

The reconciliation of the Bank's and the Group's pre-tax loss for the period to the corporate income tax expense for the period may be specified as follows:

	LVL 000's	
	2010 Group	2010 Bank
Loss before corporate income tax	(19,292)	(19,999)
Corporate income tax (at standard rate)*	(2,894)	(3,000)
Permanent differences, net	(1,120)	328
Prior year adjustments	(6)	-
Unrecognised deferred tax assets	3,539	2,100
Total effective corporate income tax	(481)	(572)

* standard rate for the period ended 31 December 2010 was 15%.

The movements in deferred corporate income tax liability can be specified as follows:

	LVL 000's	
	2010 Group	2010 Bank
As at 30 June	-	-
Restructuring	(28,867)	(29,226)
Charge to statement of income	(858)	(840)
Charge to statement of comprehensive income**	116	86
Total deferred income tax (asset) at the end of the year	(29,609)	(29,980)

Deferred corporate income tax assets and liabilities can be specified as follows:

	LVL 000's	
	2010 Group	2010 Bank
<i>Deferred tax liabilities:</i>		
Accumulated excess of tax depreciation over accounting depreciation	737	278
<i>Deferred tax assets:</i>		
Vacation pay accrual	(248)	(237)
Revaluation of securities and derivatives**	(35)	(35)
Non-taxable impairment allowance	(5,679)	(5,703)
Unutilised tax losses	(32,216)	(26,383)
Net deferred corporate income tax (asset)	(37,441)	(32,080)
Unrecognised deferred tax asset	7,832	2,100
Recognised deferred corporate income tax (asset)	(29,609)	(29,980)

** all changes in deferred tax liability that are charged directly to statement of comprehensive income are related to revaluation of securities.

Group's and Banks unutilised tax losses by expiry date can be specified as follows:

Expiry year:	LVL 000's	
	Group	Bank
2011	253	-
2012	2,295	-
2013	1,198	-
2014	634	-
2015	-	-
2016	61,494	61,494
2017	55,976	55,976
2018	55,428	55,428
Undated	27,772	2,989
Total unutilised tax losses	205,050	175,887

The movements in tax accounts of the Bank during 2010 can be specified as follows:

	LVL 000's			Balance as at 31/12/2010
	Balance as at 30/06/2010	Calculated in 2010	Paid in 2010	
Corporate income tax	-	(268)	268	-
<i>including corporate income tax withheld abroad</i>	-	(268)	268	-
Social security contributions	-	(2,061)	1,643	(418)
Personal income tax	-	(1,719)	1,718	(1)
Value added tax	-	(128)	104	(24)
Real estate tax	-	-	-	-
Total tax (payable)/ receivable	-	(4,176)	3,733	(443)

NOTE 12. CASH AND DEPOSITS WITH CENTRAL BANKS

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Cash	40,647	38,268
Deposits with the Bank of Latvia	106,472	106,472
Demand deposits with other central banks	40,101	32,608
Total cash and deposits with central banks	187,220	177,348

According to the resolution of the Council of the Bank of Latvia, credit institutions should comply with the compulsory reserve requirement calculated on the basis of attracted funding. The Bank's compulsory reserve must be exceeded by a credit institution's average monthly LVL balance on its correspondent account with the Bank of Latvia. Similar requirements also apply to the funding attracted by the Bank's branch in Estonia. During the reporting year, the Bank was in compliance with these requirements.

Demand deposits with other central banks include balances with central banks of Lithuania, Estonia, Germany and Switzerland. As at 31 December 2010, none of the amounts due from central banks were past due.

NOTE 13. BALANCES DUE FROM CREDIT INSTITUTIONS

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Due from credit institutions registered in OECD countries	155,673	127,670
Due from credit institutions registered in Latvia	57,932	54,576
Due from credit institutions registered in other non-OECD countries	6,554	29,897
Total gross balances due from credit institutions	220,159	212,143
<i>Incl. impaired balances</i>	535	535
Impairment allowance	(535)	(535)
Total net balances due from credit institutions	219,624	211,608

As at 31 December 2010, the Bank had inter-bank term deposits with 4 Latvian credit institutions and 6 OECD region credit institutions. Term deposit balances comprised 100% and 54% of total balances due from credit institutions registered in Latvia and OECD, respectively. As at 31 December 2010, none of the amounts due from credit institutions were past due.

The Bank's balances with its subsidiary AB Citadele Bankas (Lithuania) accounted for 82% of the total balances due from credit institutions registered in other non-OECD countries.

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Correspondent accounts (nostro)	65,809	62,383
Overnight deposits	26,773	34,704
Total demand deposits	92,582	97,087
<i>Term deposits with credit institutions:</i>		
due within 1 month	106,496	89,345
due within 1-3 months	6,800	12,720
due within 3-6 months	246	-
due within 6-12 months	201	-
due within 1-5 years	13,034	12,456
Over 5 years and undated	800	535
Total term deposits	127,577	115,056
Total gross balances due from credit institutions	220,159	212,143
Impairment allowance	(535)	(535)
Total net balances due from credit institutions	219,624	211,608

The above balances represent a maximum credit risk exposure to the Group and the Bank respectively.

NOTE 14. LOANS AND RECEIVABLES TO CUSTOMERS

The following table represents the current classes of loans:

	Group, LVL 000's			Bank, LVL 000's		
	31/12/2010			31/12/2010		
	Balance sheet amount	Off-balance sheet credit exposure	Total gross credit exposure	Balance sheet amount	Off-balance sheet credit exposure	Total gross credit exposure
Regular loans	649,225	6,162	655,387	560,114	5,965	566,079
Utilised credit lines	62,086	12,720	74,806	107,751	44,571	152,322
Finance leases	50,471	-	50,471	15	-	15
Debit balances on payment cards	75,187	64,816	140,003	66,583	54,573	121,156
Overdraft facilities	12,988	7,935	20,923	13,100	7,940	21,040
Loans under reverse repurchase agreements	596	-	596	-	-	-
Factoring	304	-	304	-	-	-
Due from investment and brokerage firms	4,105	-	4,105	4,058	-	4,058
Total loans and receivables to customers	854,962	91,633	946,595	751,621	113,049	864,670
Impairment allowance	(60,633)	-	(60,633)	(60,523)	-	(60,523)
Total net loans and receivables to customers	794,329	91,633	885,962	691,098	113,049	804,147

Off-balance sheet credit exposure comprises various committed financing facilities to the borrowers.

The table below provides information about loans with renegotiated terms:

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Carrying amount of restructured loans	<u>96,722</u>	<u>90,200</u>

Loans and advances by customer profile may be specified as follows:

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Private individuals	417,441	293,813
Privately held companies	386,000	415,493
State owned enterprises	22,745	18,814
Municipality owned enterprises	13,450	12,741
Public and religious institutions	11,739	7,767
Local municipalities	3,585	2,991
Government	2	2
Total gross loans and receivables to customers	854,962	751,621
Impairment allowance	(60,633)	(60,523)
Total net loans and receivables to customers	794,329	691,098

The borrowers' industry analysis of the gross portfolio of loans and receivables to corporate customers before impairment allowance may be specified as follows:

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Transport and communications	124,208	109,348
Real estate purchase and management	108,337	146,984
Trade	65,409	49,529
Hotels, restaurants	40,214	38,025
Manufacturing	24,622	20,982
Construction	13,837	9,620
Financial intermediation	11,401	58,285
Agriculture and forestry	10,805	2,148
Electricity, gas and water supply	3,650	3,008
Other industries	35,038	19,879
Total gross loans and receivables to corporate customers	437,521	457,808

The following table represents geographical profile of the portfolio of loans and receivables to customers analysed by the place of customers' reported residence:

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Latvian residents	479,977	533,202
OECD region residents	53,861	49,987
Non-OECD region residents	321,124	168,432
Total gross loans and receivables to customers	854,962	751,621
Impairment allowance	(60,633)	(60,523)
Total net loans and receivables to customers	794,329	691,098

NOTE 15. LEASES

The following table represents finance leases analysed by type of assets:

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Transport vehicles	41,236	15
Manufacturing equipment	4,426	-
Real estate	1,067	-
Other	3,742	-
Total present value of finance lease payments, excluding impairment	50,471	15
Impairment allowance	(6,432)	-
Net present value of finance lease payments	44,039	15

The following table represents reconciliation between the gross investment in the finance leases and the present value of minimum lease payments receivable:

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Gross investment in finance leases receivable:		
within 1 year	10,869	12
later than 1 year and no later than in 5 years	41,617	3
later than in 5 years	1,970	-
Total gross investment in finance leases	54,456	15
Unearned finance income receivable:		
within 1 year	668	-
later than 1 year and no later than in 5 years	3,220	-
later than in 5 years	97	-
Total	3,985	-
Present value of minimum lease payments receivable:		
within 1 year	10,201	12
later than 1 year and no later than in 5 years	38,397	3
later than in 5 years	1,873	-
Total	50,471	15

NOTE 16. FIXED INCOME SECURITIES

The Group's fixed income securities are further split as follows:

	LVL 000's			
	31/12/2010			
	Held to maturity	Available for sale	Held for trading	Total
Government bonds	117,688	119,622	63	237,373
Municipality bonds	1,726	721	-	2,447
Credit institution bonds	854	33,937	73	34,864
Corporate bonds	1,345	19,055	4	20,404
Other financial institution bonds	5,959	14,189	-	20,148
Total net fixed income securities	127,572	187,524	140	315,236

The above table represents a maximum credit risk exposure to the Group and the Bank respectively.

The Bank's fixed income securities are further split as follows:

	LVL 000's			
	31/12/2010			
	Held to maturity	Available for sale	Held for trading	Total
Government bonds	117,280	98,539	-	215,819
Municipality bonds	-	721	-	721
Credit institution bonds	-	22,160	-	22,160
Corporate bonds	-	18,705	4	18,709
Other financial institution bonds	-	3,373	-	3,373
Total net fixed income securities	117,280	143,498	4	260,782

As at 31 December 2010, there are no Group's and Bank's securities on which payments are past due or which were restructured during the reporting period.

As at 31 December 2010, the carrying amount of the Group's and Bank's securities, which were impaired but not past due amounted to LVL 4,175 thousand.

	Group, LVL 000's
	31/12/2010
Government bonds:	
Latvia	171,705
OECD	48,043
Non-OECD	17,625
Total government bonds	237,373
Municipality bonds:	
OECD	-
Non-OECD	2,447
Total municipality bonds	2,447
Credit institution bonds:	
Latvia	4,145
OECD	28,011
Non-OECD	2,708
Total credit institution bonds	34,864
Corporate bonds (OECD and non-OECD)	20,404
Other financial institution bonds (OECD and non-OECD)	20,148
Total net fixed income securities	315,236

	<u>Bank, LVL 000's</u> <u>31/12/2010</u>
Government bonds:	
Latvia	171,705
OECD	44,114
Non-OECD	-
Total government bonds	<u>215,819</u>
Municipality bonds:	
OECD	-
Non-OECD	721
Total municipality bonds	<u>721</u>
Credit institution bonds:	
Latvia	2,824
OECD	18,631
Non-OECD	705
Total credit institution bonds	<u>22,160</u>
Corporate bonds (OECD and non-OECD)	18,709
Other financial institution bonds (OECD and non-OECD)	3,373
Total net fixed income securities	<u>260,782</u>

All fixed income securities as at 31 December 2010 are listed.

NOTE 17. SHARES AND OTHER NON-FIXED INCOME SECURITIES

The following table provides the split of the Group's and Bank's shares and other non-fixed income securities:

	<u>LVL 000's</u>	
	<u>31/12/2010</u> <u>Group</u>	<u>31/12/2010</u> <u>Bank</u>
Latvian entities' equity shares:		
listed	24	-
unlisted	-	-
Total Latvian entities' equity shares	<u>24</u>	<u>-</u>
Foreign entities' equity shares:		
listed	-	-
unlisted	68	54
Total foreign entities' equity shares	<u>68</u>	<u>54</u>
Mutual investment funds	<u>9,409</u>	<u>9,375</u>
Total shares and other non-fixed income securities	<u>9,501</u>	<u>9,429</u>

The Group possess limited information on the structure of investments in managed funds, which are managed on the behalf of investors by other financial institutions. As such, these investments are not analysed by their ultimate issuer. Investments in funds, where the Group does not possess sufficient information on portfolios' composition between fixed income securities and shares are classified as investments in shares and other non-fixed income securities.

There are no off-balance sheet commitments bearing credit risk that are related to the issuers of the above securities. Further, no payments on the above instruments are past due.

NOTE 18. INVESTMENTS IN SUBSIDIARIES AND BUSINESS COMBINATIONS

Changes in the Bank's investments in subsidiaries may be specified as follows:

	LVL 000's 2010
Balance as at 30 June 2010	-
Restructuring	15,233
Acquisitions of new a subsidiary - Citadele Bankas AB	30,809
Impairment	(2,203)
Balance as at 31 December 2010	43,839

AP Anlage & Privatbank (Switzerland) is included in the consolidation group as of restructuring date based on the provisions of the agreement on the transfer of undertaking concluded between AS Parex Banka and AS Citadele Banka on 28 July 2010. The Swiss Financial Market Supervisory authority FINMA granted the supplementary permit on 24 September 2010 and the Board of Directors of AP Anlage & Privatbank approved the transfer of shares from AS Parex Banka to AS Citadele Banka on 29 October 2010.

In 2010, the management of the Bank concluded that there is an evidence of impairment of investment in the Bank's subsidiary SIA Citadele Express Kredīts. As a result an impairment amounting to LVL 400 thousand was recognized.

On 1 August 2010 AS Citadele Bank purchased AB Citadele Bankas (Lithuania) from AS Parex Bank. Both AS Citadele Bank and AS Parex Bank are under common control by Privatisation Agency. Impairment allowance in the amount of LVL 1,803 thousand was established in Bank's statements, attributable to the investment in subsidiary. Subsequent to the purchase date, the initial price was adjusted by LVL 11,192 thousand to reflect the additional information learned after the transaction took place. See Note 36.

As at 31 December 2010 the Bank held the following investments in subsidiaries:

Company	Country of registration	Business profile	Share capital LVL 000's	The Bank's share (%)	% of total voting rights	Carrying value LVL 000's
AB Citadele bankas	Lithuania	Banking	58,100	100.0	100.0	29,006
AP Anlage & Privatbank AG	Switzerland	Banking	5,630	100.0	100.0	9,702
AS Citadele Atklātais Pensiju Fonds	Latvia	Pension fund	450	100.0	100.0	454
IPAS Citadele Asset Management	Latvia	Finance	4,150	100.0	100.0	4,151
ZAO Parex Asset Management	Russia	Finance	458	100.0	100.0	-
OOO Citadele Asset Management Ukraina	Ukraine	Finance	621	100.0	100.0	-
UAB Citadele Investiciju Valdymas	Lithuania	Finance	727	100.0	100.0	-
OU Citadele Leasing & Factoring	Estonia	Finance	351	100.0	100.0	313
UAB Citadele faktoringas ir lizingas	Lithuania	Finance	305	100.0	100.0	-
SIA Rīgas Pirmā Garāža	Latvia	Misc.*	352	100.0	100.0	-
SIA Citadele Express Kredīts	Latvia	Leasing	31	100.0	100.0	213
SIA E&P Baltic Properties	Latvia	Finance	20	50.0	50.0	-
SIA Citadele Līzings un Faktoringas	Latvia	Leasing	9,400	100.0	100.0	-
AAS Citadele Life	Latvia	Life insurance	3,000	100.0	100.0	-
Calenia Investments Limited	Cyprus	Misc.*	-	100.0	100.0	-
OOO Citadele Investments Ukraine	Ukraine	Finance	44	100.0	100.0	-
SIA RPG Interjers	Latvia	Misc.*	2	100.0	100.0	-
OAo Parex Ukrainian Equity Fund	Ukraine	Finance	-	100.0	100.0	-
SIA PR Speciālie Projekti	Latvia	Misc.*	2	100.0	100.0	-
Total investments in subsidiaries						43,839

* Misc. – the companies are providing various support services

NOTE 19. INTANGIBLE ASSETS

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Software	604	405
Other intangible assets	615	23
Total intangible assets excluding advances	1,219	428
Advances for intangible assets	841	828
Total net book value of intangible assets	2,060	1,256

Movements in the Group's intangible assets excluding advances for the six month period ended 31 December 2010 can be specified as follows:

	LVL 000's			
	Goodwill from acquisition of subsidiaries	Software	Other intangible assets	Total intangible assets excluding advances
<i>Historical cost</i>				
As at 30 June 2010	-	-	-	-
Restructuring	131	8,818	2,448	11,397
Additions	-	131	-	131
Disposals	-	(45)	(26)	(71)
Impairment allowance	(131)	-	-	(131)
As at 31 December 2010	-	8,904	2,422	11,326
<i>Accumulated amortisation</i>				
As at 30 June 2010	-	-	-	-
Restructuring	-	8,126	1,700	9,826
Charge for the year	-	219	132	351
Reversal due to disposals	-	(45)	(25)	(70)
As at 31 December 2010	-	8,300	1,807	10,107
<i>Net book value</i>				
As at 30 June 2010	-	-	-	-
As at 31 December 2010	-	604	615	1,219

NOTE 20. FIXED ASSETS

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Leasehold improvements	1,296	1,296
Land and buildings	30,204	679
Transport vehicles	912	281
Other fixed assets	5,606	1,601
Total fixed assets excluding advances	38,018	3,857
Advances for fixed assets	54	53
Total net book value of fixed assets	38,072	3,910

The following changes in the Group's fixed assets excluding advances for fixed assets took place during the 6 month period ended 31 December 2010:

	LVL 000's				
	Leasehold improve- ments	Land and buildings	Transport vehicles	Other fixed assets	Total fixed assets excluding advances
<i>Historical cost</i>					
As at 30 June 2010	-	-	-	-	-
Restructuring	3,654	35,253	2,706	25,827	67,440
Additions	17	8	359	339	723
Disposals	(4)	-	(525)	(1,082)	(1,611)
As at 31 December 2010	3,667	35,261	2,540	25,084	66,552
<i>Accumulated depreciation</i>					
As at 30 June 2010	-	-	-	-	-
Restructuring	2,011	3,751	1,887	19,389	27,038
Charge for the year	364	1,306	179	1,091	2,940
Reversal due to disposals	(4)	-	(438)	(1,002)	(1,444)
As at 31 December 2010	2,371	5,057	1,628	19,478	28,534
<i>Net book value (incl .impairment allowance)</i>					
As at 30 June 2010	-	-	-	-	-
As at 31 December 2010	1,296	30,204	912	5,606	38,018
<i>Impairment allowance</i>					
As at 30 June 2010	-	-	-	-	-
Restructuring	-	(17,915)	-	-	(17,915)
As at 31 December 2010	-	(17,915)	-	-	(17,915)

The following changes in the Bank's fixed assets excluding advances for fixed assets took place during the 6 month period ended 31 December 2010:

	LVL 000's				Total fixed assets excluding prepayments
	Leasehold Improvements	Land and buildings	Transport vehicles	Other fixed assets	
<i>Historical cost</i>					
As at 30 June 2010	-	-	-	-	-
Restructuring	3,654	814	1,581	18,443	24,492
Additions	17	-	-	241	258
Disposals	(4)	-	(142)	(498)	(644)
As at 31 December 2010	3,667	814	1,439	18,186	24,106
<i>Accumulated depreciation</i>					
As at 30 June 2010	-	-	-	-	-
Restructuring	2,011	129	1,227	16,517	19,884
Charge for the year	364	6	73	566	1,009
Reversal due to disposals	(4)	-	(142)	(498)	(644)
As at 31 December 2010	2,371	135	1,158	16,585	20,249
<i>Net book value</i>					
As at 30 June 2010	-	-	-	-	-
As at 31 December 2010	1,296	679	281	1,601	3,857

NOTE 21. NON-CURRENT ASSETS HELD FOR SALE

	LVL 000's 31/12/2010 Group
Transport vehicles	4,827
Total gross non-current assets held for sale	4,827
Impairment allowance	(1,538)
Total net non-current assets held for sale	3,289
	LVL 000's 31/12/2010 Group
Net carrying amount at the beginning of the period	-
Restructuring - initial carrying amount	6,425
Restructuring - impairment allowance	(2,256)
Restructuring - net carrying amount	4,169
Impairment charges	(338)
Impairment reversals	352
Decrease of impairment allowance due to disposals	703
Net impairment charge to income statements	717
Increase of initial carrying amount due to additions	1,212
Decrease of initial carrying amount due to disposals	(2,809)
Net change in initial carrying amount	(1,597)
Initial carrying amount as at the end of the year	4,828
Impairment allowance at the end of the year	(1,539)
Net carrying amount at the end of the year	3,289

NOTE 22. OTHER ASSETS

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Money in transit	1,970	1,957
Prepayments	779	610
Accrued income *	773	142
VAT receivables	293	244
Other assets *	2,787	1,309
Total gross other assets	6,602	4,262
Impairment allowance	(611)	(326)
Total net other assets	5,991	3,936

* As at 31 December 2010, included in the Group's and Bank's other assets and accrued income are assets amounting to LVL 902 thousand and LVL nil, respectively, which are delayed. Additionally, as at 31 December 2010, the Group's and the Bank's other assets amounts that are not delayed but impaired amount to LVL 344 thousand and LVL 326 thousand, respectively.

NOTE 23. ISSUED DEBT SECURITIES

As at 31 December 2010, the Bank had the following outstanding debt issues:

Issue date	Issue amount	Coupon	Payment, frequency	Maturity	Debt outstanding (LVL 000's)
					31/12/2010
May, 2007	EUR 200 million	5.625%	Annual	May, 2011	70,573
February and June, 2010	EUR 29.3 million	5%	Semi annual	February, 2012	20,984
Total					91,557

NOTE 24. BALANCES DUE TO CREDIT INSTITUTIONS AND CENTRAL BANKS

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Due to credit institutions registered in OECD countries	8,318	16,830
Due to credit institutions registered in Latvia	57,664	56,557
Due to credit institutions registered in other non-OECD countries	4,577	8,788
Total balances due to credit institutions and central banks	70,559	82,175

The following table presents the Group's and Bank's balances due to credit institutions and central banks according to maturity profile:

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Balances on demand	58,668	58,216
Overnight deposits	-	8,434
Total balances repayable on demand	58,668	66,650
Loans from credit institutions:		
due within 1 month	4,862	4,711
due within 1-3 months	7,029	10,199
due within 3-6 months	-	615
Total loans from credit institutions	11,891	15,525
Total due to credit institutions	70,559	82,175

The Bank has concluded a repo transaction, whereby it pledged part of the securities portfolio against the financing received. Please refer to Note 31 for more details.

NOTE 25. DEPOSITS FROM CUSTOMERS

The following table presents deposits from customers according to customer profile:

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Privately held companies	526,916	436,166
Private individuals	436,484	353,354
Government	173,684	171,707
State owned enterprises	88,835	88,648
Financial institutions	37,314	37,311
Municipalities	26,240	26,229
Public and religious institutions	4,862	3,859
Total deposits from customers	1,294,335	1,117,274

Financing support from the Ministry of Finance

According to EU restructuring plan a certain amount of State support was transferred to the Bank. Ministry of Finance of Latvia has made a number of deposits on a secured basis, receiving part of Bank's loan portfolio as collateral (please refer to Note 31 for details on assets pledged). As at 31 December 2010, the following financing support received from the Ministry of Finance was outstanding:

Agreement currency	Interest rate (%)	Agreement date	Maturity date	Amortised cost LVL 000's 31/12/2010
EUR	10.003	01/08/2010	30/06/2011	32,751
EUR	10.003	01/08/2010	30/09/2011	32,751
EUR	10.003	01/08/2010	30/12/2011	32,750
EUR	10.003	01/08/2010	30/03/2012	32,748
Total Treasury deposits				131,000

Subsequent to the balance sheet date the Bank has repaid EUR 46.6 million ahead of the schedule from the State support deposits outstanding. Please refer to Note 36 for more information.

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Demand deposits	516,872	416,633
Term deposits:		
due within 1 month	169,440	149,798
due within 1-3 months	163,546	144,016
due within 3-6 months	141,754	120,632
due within 6-12 months	152,419	138,317
due within 1-5 years	149,826	147,448
due in more than 5 years	478	430
Total term deposits	777,463	700,641
Total deposits from customers	1,294,335	1,117,274

NOTE 26. OTHER LIABILITIES

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Accrued expense	4,817	3,984
Suspense liabilities	1,663	1,663
Amounts due to suppliers	1,176	801
Provisions for other liabilities	319	-
VAT payables	203	26
Deferred income	31	-
Other liabilities	4,519	2,445
Total other liabilities	12,728	8,919

Suspense liabilities comprise funds received by the Group and the Bank as at year end, but not yet transferred to ultimate beneficiaries due to unclear or incomplete details of the supporting documentation.

NOTE 27. SUBORDINATED DEBT

The following table represents the details of Bank's and Group's subordinated capital:

Counterparty	Residence country	Currency	Issue size, 000's	Interest rate	Original agreement date	Original maturity date	Amortised cost (LVL 000's) 31/12/2010
Privatisation Agency	Latvia	EUR	53,128	20.861%	22/05/2009	21/05/2016	38,008
Privatisation Agency	Latvia	EUR	11,205	8.152%	02/08/2010	08/08/2016	8,128
EBRD	UK	EUR	7,195	8.152%	11/09/2009	08/08/2016	5,099
Total							51,235

NOTE 28. ISSUED SHARE CAPITAL

As at 31 December 2010, the Bank's registered and paid-in share capital was LVL 103,000 thousand. In accordance with the Bank's statutes, the share capital consists of 103,000 thousand ordinary shares with voting rights. All shares have a par value of LVL 1 each and, as at 31 December 2010, they all were issued and fully paid. As at 31 December 2010, the Bank did not possess any of its own shares. No dividends were proposed and paid during 2010.

As at 31 December 2010, the Bank had 2 shareholders. The respective shareholdings as at 31 December 2010 may be specified as follows:

	31/12/2010		
	Paid-in share capital (LVL)	% of total paid-in capital	% of total voting rights
Privatisation Agency	77,249,999	75% minus 1 share	75% minus 1 share
European Bank for Reconstruction and Development	25,750,001	25% plus 1 share	25% plus 1 share
Total	103,000,000	100.00	100.00

AS Citadele Banka was established by *Privatisation Agency* on 30 June 2010 with initial paid-in share capital of LVL 4 million.

Capital increases

On 29 July 2010 the Bank's capital was further increased by LVL 99 million to LVL 103 million. The increase was carried out by the sole shareholder of the Bank *Privatisation Agency* by purchase of a corresponding amount of voting shares.

Changes in the shareholding structure

On 30 July 2010, *European Bank for Reconstruction and Development* (EBRD) concluded a share purchase agreement with *Privatisation Agency*, whereby the EBRD became part owner of Citadele's shareholding structure with 25 % of share capital plus 1 voting share.

NOTE 29. OFF-BALANCE SHEET ITEMS

Memorandum items comprise contingent liabilities, financial commitments, foreign exchange contracts and derivative financial instruments. The following table provides a specification of contingent liabilities (showing maximum amount payable) and financial commitments outstanding as at 31 December 2010.

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Contingent liabilities:		
Outstanding guarantees	9,893	6,706
Outstanding letters of credit	235	18
Total contingent liabilities	10,128	6,724
Financial commitments:		
Loans granted, not fully drawn down	6,162	5,965
Unutilised credit lines and overdraft facilities	20,655	52,511
Credit card commitments	64,816	54,573
Total financial commitments	91,633	113,049

The following table presents the notional amounts and fair values of foreign exchange contracts and derivative financial instruments. The notional amounts of foreign exchange contracts represent the amounts receivable under these contracts. The notional amounts of other financial instruments represent the value of the underlying assets.

The Group:

	Notional amount LVL 000's 31/12/2010	Fair value	
		LVL 000's 31/12/2010	
		Assets	Liabilities
Foreign exchange contracts:			
Spot exchange	20,122	144	(359)
Forwards	54,492	88	(66)
Swaps	457,053	2,378	(193)
Total foreign exchange contracts	531,667	2,610	(618)
Other financial instruments:			
Other derivatives	7,028	60	(26)
Total other financial instruments	7,028	60	(26)
Derivative financial instruments	538,695	2,670	(644)

The Bank:

	Notional amount LVL 000's 31/12/2010	Fair value	
		LVL 000's 31/12/2010	
		Assets	Liabilities
Foreign exchange contracts:			
Spot exchange	9,430	144	(363)
Forwards	77,337	147	(58)
Swaps	465,898	2,365	(255)
Total foreign exchange contracts	552,665	2,656	(676)
Other financial instruments:			
Other derivatives	7,028	60	(26)
Total other financial instruments	7,028	60	(26)
Derivative financial instruments	559,693	2,716	(702)

The Group's banks use derivative foreign exchange instruments to manage their currency positions, which arise also due to derivative foreign exchange contracts concluded with the banks' clients. Before entering into derivative foreign currency agreement with private individual or company, the Group's entities assess the counterparty's ability to meet the contractual provisions. As at 31 December 2010, more than 92% of the fair value assets on foreign exchange contracts is attributable to credit and finance institutions. As at 31 December 2010, none of the payments receivable arising out of derivative transactions was past due.

NOTE 30. FUNDS UNDER TRUST MANAGEMENT

The table below provides analysis of the fair value of funds managed on behalf of customers by investment type:

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Fixed income securities:		
Government bonds	41,909	-
Credit institution bonds	41,626	-
Corporate bonds	38,062	-
Foreign municipality bonds	1,711	-
Other financial institution bonds	4,307	-
Total investments in fixed income securities	127,615	-
Other investments:		
Mutual investment funds	78,087	-
Deposits with credit institutions	59,714	-
Shares	38,937	1
Real estate	19,273	-
Loans to corporate entities	2,955	774
Other	32,194	-
Total other investments	231,160	775
Total assets under trust management agreements	358,775	775

The table below provides an analysis of the customer profile on whose behalf the funds are managed:

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Investors of investment funds	231,442	-
Privately held companies	69,494	774
Private individuals	57,067	1
Financial institutions	772	-
Total liabilities under trust management agreements	358,775	775

NOTE 31. FINANCIAL ASSETS PLEDGED

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Due from credit institutions*	25,839	25,839
<i>Held for trading securities</i>	3,174	3,174
<i>Available-for-sale securities</i>	4,764	4,764
Total securities pledged	7,938	7,938
Loans to customers	178,804	178,804
Total financial assets pledged	212,581	212,581
Due to credit institutions and central banks	7,028	7,028
Deposits from Ministry of Finance	131,000	131,000
Total liabilities secured by pledged financial assets	138,028	138,028

* The amount consists of several placements to secure various Bank's transactions in the ordinary course of business.

As at 31 December 2010, the Bank has entered into repo agreement with European Central Bank, whereby it pledged part of its securities portfolio against the financing facilities received.

Further, the Bank has concluded several agreements with Ministry of Finance of Latvia, whereby it pledged part of the loan portfolio as a security to the financing received. The respective pledges are registered with Commercial Register. Please refer to Note 25 for more detailed information on deposits received from the Ministry of Finance.

NOTE 32. CASH AND CASH EQUIVALENTS

The table below provides a breakdown of cash and cash equivalents as at 31 December 2010:

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
Cash and demand deposits with central banks	187,220	177,348
Deposits with other credit institutions*	205,465	199,152
Demand deposits due to other credit institutions	(58,668)	(66,650)
Total cash and cash equivalents	334,017	309,850

* Deposits include term facilities with initial agreement term of 3 months or less.

NOTE 33. LITIGATION AND CLAIMS

In the ordinary course of business, the Bank has been involved in a number of legal proceedings to recover collateral or outstanding credit balances, as well as related interest and expenses from defaulted credit customers and interbank counterparties. The Group is also involved in a number of legal proceedings related to its customers in Latvia and abroad.

The management of the Bank believes that any legal proceedings pending as at 31 December 2010 will not result in material losses for the Group.

NOTE 34. RELATED PARTIES

Related parties are defined as shareholders who have significant influence over the Group, state and municipal institutions, members of the Council and Management Board, key Management personnel, their close relatives and companies in which they have a controlling interest as well as associated companies of the Group. For the purpose of this disclosure, the key management of the Group's companies/ Bank and their related companies are stated in one line, accordingly.

The Bank of Latvia is not considered as related party as it is operating as an independent institution according to special law.

The following table present the outstanding balances and terms of the Group's transactions with counterparties, which were related parties as at 31 December 2010.

	Amount in LVL 000's 31/12/2010	Interest income/ expense 30/06/2010- 31/12/2010
Credit exposure to related parties		
Securities:	171,705	3,488
<i>Latvian treasury bills and government bonds</i>	171,705	3,488
Loans and receivables:		
<i>Management</i>	3,637	35
<i>Municipality institutions</i>	646	7
	2,991	28
Financial commitments and outstanding guarantees:		
<i>Management</i>	4,226	-
<i>State institutions</i>	46	-
<i>Municipality institutions</i>	3,170	-
	1,010	-
Total credit exposure to related parties	179,568	
Due to related parties:		
<i>Deposits from Ministry of Finance</i>	247,953	10,188
<i>Subordinated loans from shareholder</i>	131,000	5,581
<i>Management</i>	51,235	3,766
<i>State institutions</i>	530	10
<i>Municipality institutions</i>	39,230	767
	25,958	64
Total amounts due to related parties	247,953	

No Group's exposures with related parties as at 31 December 2010 or for the 6 month period then ended were impaired.

The following table presents the outstanding balances and terms of the Bank's transactions with counterparties, which were related parties as at 31 December 2010.

	Gross amount in LVL 000's 31/12/2010	Interest income/ expense 30/06/2010- 31/12/2010
Credit exposure to related parties		
Securities:	171,705	3,488
<i>Latvian treasury bills and government bonds</i>	<i>171,705</i>	<i>3,488</i>
Loans and receivables:	133,856	1,533
<i>Management</i>	<i>160</i>	<i>2</i>
<i>Municipality institutions</i>	<i>2,991</i>	<i>28</i>
<i>Subsidiaries</i>	<i>130,705</i>	<i>1,503</i>
Derivatives – assets:	71	-
<i>Subsidiaries</i>	<i>71</i>	<i>-</i>
Financial commitments and outstanding guarantees:	37,221	
<i>Management</i>	<i>46</i>	
<i>State institutions</i>	<i>3,170</i>	
<i>Municipality institutions</i>	<i>1,010</i>	
<i>Subsidiaries</i>	<i>32,995</i>	
Total credit exposure to related parties	<u>342,853</u>	
Due to related parties:	269,353	10,321
<i>Deposits from Ministry of Finance</i>	<i>131,000</i>	<i>5,581</i>
<i>Subordinated loans from shareholders</i>	<i>51,235</i>	<i>3,766</i>
<i>Management</i>	<i>216</i>	<i>12</i>
<i>State institutions</i>	<i>39,230</i>	<i>767</i>
<i>Municipality institutions</i>	<i>25,958</i>	<i>64</i>
<i>Subsidiaries</i>	<i>21,714</i>	<i>131</i>
Derivatives – liabilities:	71	-
<i>Subsidiaries</i>	<i>71</i>	<i>-</i>
Total amounts due to related parties	<u>269,424</u>	

In the 6 month period ended 31 December 2010 the Bank has recognized a net impairment allowance of LVL 2,352 thousand on loans and receivables from subsidiaries. As at 31 December 2010 the total impairment allowance recognized on loans and receivables from subsidiaries was LVL 16,410 thousand. No other Bank's exposures with related parties as at 31 December 2010 or for the 6 month period then ended were impaired.

NOTE 35 RISK MANAGEMENT

Risk management polices

Risk management principles are set out in Group's Risk and Capital Management Policy (as approved by the Supervisory Board and Management Board). The Group adheres to the following key risk management principles:

- The Group aims to ensure low risk exposure, diversified asset portfolio, limited risks in financial markets and low level of operational risk;
- The Group aims to ensure an acceptable risk level in all operations. Risks are always assessed in relation to the expected return. Risk exposures that are not acceptable for the Group are avoided, limited or hedged;
- The Group does not assume high or uncontrollable risks irrespective of the return they provide. Risks should be diversified and those risks that are quantifiable should be limited or hedged;
- The Group pursues prudent risk management policy, that is aligned with the Group' business and ensures effective total risk mitigation;
- Risk management is based on awareness of each and every Group's employee about the nature of transactions he/she carries out and related risks;
- Risk limit system and strict controls are essential risk management elements. Control of risk level and compliance with limits is ensured by structured risk limit systems for all material risks.

Risk management is an essential element of the Group's management process. Risk management within the Group is controlled by independent units – Risk and Compliance Sector.

The Group is exposed to the following main risks: credit risk, market risk, interest rate risk, liquidity risk and operational risk. The Group has approved risk management policies for each of these risks, which are briefly summarised below.

a) Credit risk

Credit risk is the risk that the Group will incur a loss from debtor's non-performance or default. The group is exposed to credit risk in its lending, investing and trading activities, as well as in respect to the guarantees issued to third parties and other off-balance sheet commitments to third parties.

Credit risk management is based on adequate risk assessment and decision-making. For material risks, risk analysis is conducted by independent units of Risk and Compliance Sector. The analysis of credit risk comprises evaluation of customer's creditworthiness and collateral and its liquidity. The analysis of creditworthiness of a legal entity includes analysis of the industry, the company, and its current and forecasted financial position. The analysis of creditworthiness of an individual includes the analysis of the customer's credit history, income and debt-to-income ratio analysis, as well as the analysis of social and demographic factors. In the event of material risks, lending decision is made by the Credit Committee, and further reviewed by the Bank's Management Board.

After the loan is issued, customer's financial position is monitored on a regular basis in order to timely identify potential credit losses.

To limit its credit risk, the Group has set the following concentration limits: individual counterparty limit, limit for group of mutually related customers, limit for large risk exposures, limit for the Group's related parties, an industry limit, limit by customer type, loan product and type of collateral.

The Group reviews its loan portfolio on a regular basis to assess its quality and concentrations, as well as to evaluate the portfolio trends.

Credit risk identification, monitoring and reporting is the responsibility of Risk and Compliance Sector.

The tables below provide details of the Group's loan portfolio delinquencies:

	Group, LVL 000's								
	Regular loans	Utilised credit lines	Finance leases	Debit balances on settlement cards	31/12/2010 Loans under reverse repurchase agreement	Overdraft facilities	Factoring	Due from investment and brokerage firms	Total
Not delayed - not impaired	529,233	58,635	32,257	50,601	596	12,140	11	3,552	687,025
<i>Incl. restructured loans</i>	<i>75,918</i>	<i>6,496</i>	<i>472</i>	-	-	-	-	-	<i>82,886</i>
Not delayed - impaired	18,953	-	460	-	-	-	4	-	19,417
Total not delayed loans	548,186	58,635	32,717	50,601	596	12,140	15	3,552	706,442
Past due loans - not impaired									
Delayed days:									
=< 29	35,377	606	7,336	1,033	-	-	-	-	44,352
30-59	14,980	-	2,480	576	-	-	-	-	18,036
60-89	4,339	-	194	484	-	-	-	-	5,017
90 and more	19,825	2,408	313	3,807	-	25	-	-	26,378
Total past due loans - not impaired	74,521	3,014	10,323	5,900	-	25	-	-	93,783
Total past due loans - impaired	26,518	437	7,431	18,686	-	823	289	553	54,737
Total gross loans and receivables to customers	649,225	62,086	50,471	75,187	596	12,988	304	4,105	854,962
Impairment allowance	(29,319)	(1,297)	(6,432)	(21,749)	-	(951)	(292)	(593)	(60,633)
Total net loans and receivables to customers	619,906	60,789	44,039	53,438	596	12,037	12	3,512	794,329

Mostly, not-delayed loans falling into categories "regular loans" and "utilised credit lines" are secured by collateral. More than 77% are secured by real estate collateral. In general, settlement card loans are granted to clients on a basis of their cash flows' assessment and no collateral is required in most cases. Finance leases are secured by the respective property leased out (for more details on leasing portfolio please refer to Note 15). Loans under reverse repurchase agreements are secured with securities that can be sold in case of client's default.

As at 31 December 2010, included in the loan portfolio are not delayed impaired loans, not impaired past due loans and impaired past due loans with the estimated value of collateral amounting to approximately LVL 16 million, LVL 125 million and LVL 15 million respectively.

The tables below provide details of the Bank's loan portfolio delinquencies:

	Bank, LVL 000's								
	Regular loans	Utilised credit lines	Finance leases	Debit balances on settlement cards	31/12/2010 Loans under reverse repurchase agreement	Overdraft facilities	Factoring	Due from investment and brokerage firms	Total
Not delayed - not impaired	414,088	61,563	10	45,060	-	12,252	-	3,505	536,478
<i>Incl. restructured loans</i>	<i>73,248</i>	<i>5,899</i>	-	-	-	-	-	-	<i>79,147</i>
Not delayed - impaired	63,963	43,720	-	-	-	-	-	-	107,683
Total not delayed loans	478,051	105,283	10	45,060	-	12,252	-	3,505	644,161
Past due loans - not impaired									
Delayed days:									
=< 29	26,880	60	5	610	-	-	-	-	27,555
30-59	13,772	-	-	463	-	-	-	-	14,235
60-89	3,993	-	-	399	-	-	-	-	4,392
90 and more	15,893	2,408	-	1,365	-	25	-	-	19,691
Total past due loans - not impaired	60,538	2,468	5	2,837	-	25	-	-	65,873
Total past due loans - impaired	21,525	-	-	18,686	-	823	-	553	41,587
Total gross loans and receivables to customers	560,114	107,751	15	66,583	-	13,100	-	4,058	751,621
Impairment allowance	(35,449)	(4,193)	-	(19,337)	-	(951)	-	(593)	(60,523)
Total net loans and receivables to customers	524,665	103,558	15	47,246	-	12,149	-	3,465	691,098

The following table provides details on changes in the Group's specific loan portfolio impairment by classes:

	Regular loans	Utilised credit lines	Finance leases	Debit balances on settlement cards	Overdraft facilities	Factoring	Due from investment and brokerage firms	Total
Outstanding specific impairment as at 30/06/2010	-	-	-	-	-	-	-	-
Restructuring	14,097	847	4,779	16,595	452	239	505	37,514
Impairment charge for the reported period - specific	8,730	190	1,819	2,091	370	1	-	13,201
Release of previously established impairment allowance - specific	(2,391)	(45)	(319)	-	-	-	-	(2,755)
Impairment charged to the statement of income, net	6,339	145	1,500	2,091	370	1	-	10,446
Change of impairment allowance due to write-offs, net	(25)	(787)	(243)	-	-	-	-	(1,055)
Increase/ (decrease) in impairment allowance due to currency fluctuations	(8)	39	(80)	-	1	-	48	-
Outstanding specific impairment as at 31/12/2010	20,403	244	5,956	18,686	823	240	553	46,905

The following table provides details on changes in the Bank's specific loan portfolio impairment by classes:

	Regular loans	Utilised credit lines	Finance leases	Debit balances on settlement cards	Overdraft facilities	Factoring	Due from investment and brokerage firms	Total
Outstanding specific impairment as at 30/06/2010	-	-	-	-	-	-	-	-
Restructuring	26,306	793	-	16,595	452	-	505	44,651
Impairment charge for the reported period - specific	6,819	2,352	-	2,091	370	-	-	11,632
Release of previously established impairment allowance - specific	(2,373)	-	-	-	-	-	-	(2,373)
Impairment charged to the statement of income, net	4,446	2,352	-	2,091	370	-	-	9,259
Change of impairment allowance due to write-offs, net	(756)	-	-	-	-	-	-	(756)
Increase/ (decrease) in impairment allowance due to currency fluctuations	-	-	-	-	1	-	48	49
Outstanding specific impairment as at 31/12/2010	29,996	3,145	-	18,686	823	-	553	53,203

The tables below provide details of the Group's and Bank's securities portfolio quality:

Group, LVL 000's				
31/12/2010				
	Held to maturity	Available for sale	Held for trading	Total
Investment grade:				
AAA	-	66,091	-	66,091
AA	-	11,009	-	11,009
A	5,241	11,927	-	17,168
BBB/Baa	112,075	48,881	63	161,019
Other lower ratings	10,256	49,616	9	59,881
Not rated	-	-	68	68
Total net fixed income securities	127,572	187,524	140	315,236

Bank, LVL 000's				
31/12/2010				
	Held to maturity	Available for sale	Held for trading	Total
Investment grade:				
AAA	-	59,167	-	59,167
AA	-	2,104	-	2,104
A	-	4,847	-	4,847
BBB/Baa	108,104	29,329	-	137,433
Other lower ratings	9,176	48,051	4	57,231
Total net fixed income securities	117,280	143,498	4	260,782

GEOGRAPHICAL PROFILE

The following tables provide an analysis of the Group's and Bank's assets and liabilities, as well as memorandum items outstanding as at 31 December 2010 by geographical profile. The grouping by is done based on information about the residence of the respective counterparties.

	Group as at 31/12/2010, LVL 000's					Total
	Latvia	Lithuania	Other EU countries	CIS countries	Other countries	
Assets						
Cash and deposits with central banks	141,835	7,987	35,513	-	1,885	187,220
Balances due from credit institutions	55,483	356	106,821	5,676	51,288	219,624
Securities held for trading	170	-	4	-	-	174
Financial assets designated at fair value through profit or loss	1,796	408	1,113	-	1	3,318
Available-for-sale securities	60,868	16,170	73,910	17,095	28,948	196,991
Loans and receivables to customers	432,738	163,385	63,569	87,647	46,990	794,329
Held-to-maturity securities	117,280	-	179	3,786	6,327	127,572
Derivatives financial instruments	2,249	26	57	25	313	2,670
Other assets	73,752	5,497	757	430	175	80,611
Total assets	886,171	193,829	281,923	114,659	135,927	1,612,509
Liabilities						
Financial liabilities designated at fair value through profit or loss	1,484	-	-	-	-	1,484
Financial liabilities measured at amortised cost	813,297	106,618	221,498	12,418	361,116	1,514,947
Derivative financial instruments	222	12	285	13	112	644
Other liabilities	10,652	1,337	386	17	1,015	13,407
Total liabilities	825,655	107,967	222,169	12,448	362,243	1,530,482
Equity	82,027	-	-	-	-	82,027
Total liabilities and equity	907,682	107,967	222,169	12,448	362,243	1,612,509
Memorandum items						
Contingent liabilities	3,254	2,561	114	2,882	1,317	10,128
Financial commitments	71,886	11,352	283	7,705	407	91,633

	Bank as at 31/12/2010, LVL 000's					Total
	Latvia	Lithuania	Other EU countries	CIS countries	Other countries	
Assets						
Cash and deposits with central banks	141,835	-	35,513	-	-	177,348
Balances due from credit institutions	54,577	24,612	92,455	4,614	35,350	211,608
Securities held for trading	-	-	4	-	-	4
Available-for-sale securities	59,513	-	60,583	13,570	19,261	152,927
Loans and receivables to customers	476,343	24,061	60,653	87,539	42,502	691,098
Held-to-maturity securities	117,280	-	-	-	-	117,280
Derivatives financial instruments	2,249	71	57	25	314	2,716
Other assets	82,646	-	180	10	85	82,921
Total assets	934,443	48,744	249,445	105,758	97,512	1,435,902
Liabilities						
Financial liabilities measured at amortised cost	814,555	9,223	202,676	1,003	314,784	1,342,241
Derivative financial instruments	221	71	285	13	112	702
Other liabilities	8,594	1	317	6	1	8,919
Total liabilities	823,370	9,295	203,278	1,022	314,897	1,351,862
Equity	84,040	-	-	-	-	84,040
Total liabilities and equity	907,410	9,295	203,278	1,022	314,897	1,435,902
Memorandum items						
Contingent liabilities	3,101	365	44	2,882	332	6,724
Financial commitments	97,951	6,708	283	7,704	403	113,049

b) Market risk

Market risk is the risk that the Group will incur a loss as a result of the mark-to-market revaluation of balance sheet and off-balance sheet items caused by changes in market values of financial instruments, commodities and commodity derivatives due to changes in foreign exchange rates, interest rates and other factors.

Position risk of financial instruments is assessed and limits are set by the Financial Market and Counterparty Committee (FMCC). The decisions of FMCC are approved by the Bank's Management Board. Market risk is managed by the Group's business units and subsidiaries which can accept market risk in line with the set limits and investment restrictions of the respective portfolio. Market risk is measured, monitored and risk levels are reported by Risk and Compliance Sector.

To assess the position risk, scenario analysis is applied. Scenario analysis is based on historic data and price changes of various financial instruments in different low probability high impact scenarios. For example, a flight-to-quality scenario assumes that investors move their capital from riskier investments towards safer investments (for instance, U.S. or other AAA-rated sovereign bonds). To manage market risk, the Group sets individual limits to issuers and financial instruments, as well as products exposed to market risk.

c) Equity price risk

Equity price risk is the risk that the Group will incur a loss due to changes in equity prices. Equity price risk is assessed and decisions on limits set are made by the Financial Market and Counterparty Committee. Further the decisions so made are approved by the Bank's Management Board.

To assess equity price risk, the Group applies the scenario analysis "flight-to-quality" which refers to a fear of investors of global systemic failure when investors start selling assets they consider to be overly risky and substituting them with more dependable ones. According to the Bank's equity price risk assessment as at 31 December 2010, in the event that all equity (also including investments in investment funds) prices drop by 10% for equities in OECD countries, 20% – Baltic countries and CIS countries and 15% – other equities, revaluation loss charged directly to the equity would increase by approximately LVL 1.1 million and an impairment loss of LVL 0.4 million would be recognized in the income statement.

d) Interest rate risk

Interest rate risk is related to the negative impact of interest rate changes on the Group's income and economic value.

Interest rate risk management in the Group is carried out in accordance with the Group's Interest rate Risk Management Policy. Interest rate risk is assessed and decisions are made by Assets and Liabilities Management Committee (ALCO). The decisions of ALCO are approved by the Bank's Management Board. ALCO sets the acceptable interest rate risk level and the Group's internal limit system, monitors the compliance with the approved limits and use of the instruments for the management of interest rate risk. Interest rate risk measurement and management is the responsibility of Treasury Sector, while risk reporting is the responsibility of Risk and Compliance Sector.

The Group manages interest rate risk by using the gap analysis of the risk sensitive assets and liabilities, duration analysis and sensitivity analysis of assets and liabilities as well as stress testing of interest rate risk. Based on the market analysis and the Group's financing structure, ALCO sets customer deposit interest rates. Partially, the Group mitigates interest rate risk using derivatives.

The following table represents the impact of a parallel change in all interest rates by 1.0% on Group's and Bank's pre-tax profit (in 12-months time) and available-for-sale securities' fair value revaluation reserve in equity:

	LVL 000's	
	2010 Group	2010 Bank
Scenario: +1%		
Pre-tax profit/ (loss)	(1,829)	(1,699)
Securities fair value revaluation reserve	(1,620)	(1,620)
Total pre-tax effect on equity	(3,449)	(3,319)
Estimated net effect on equity	(2,932)	(2,821)
Scenario: -1%		
Pre-tax profit	2,001	1,864
Securities fair value revaluation reserve	1,710	1,710
Total pre-tax effect on equity	3,711	3,574
Estimated net effect on equity	3,154	3,038

FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES

The concept of fair value assumes realisation of financial instruments by way of a sale. However, in many cases, particularly in respect of loans and receivables to customers, the Group intends to realise assets through collection over time. Users of these financial statements are therefore advised to use caution when using this data to evaluate the Group's financial position.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable and willing parties in an arm's length transaction. The fair value of liquid financial assets has been determined using bid prices, while offer prices have been used to determine the fair value of financial liabilities.

For illiquid financial assets and liabilities, including loans and advances to customers, there are, by definition, no active markets. Accordingly, fair value has been estimated using appropriate valuation techniques. The methods used to determine the fair value of balance sheet items not carried at fair value are as follows:

Cash and demand deposits with central banks

The fair value of cash and balances with central banks is their carrying amount as these balances may be withdrawn without notice.

Balances due from credit institutions/ Balances due to credit institutions and central banks

The fair value of on-demand balances with credit institutions is their carrying amount as these balances may be withdrawn without notice. The fair value of overnight placements is their carrying amount. The fair value of other amounts due from banks is calculated by discounting expected cash flows using current market rates. In many cases, the carrying value is a close representation of fair value due to short-term maturity profiles.

Loans and receivables to customers

The fair value of loans and advances to customers is calculated by discounting expected future cash flows. The discount rates consist of money market rates as at the end of year and credit margins, which are adjusted for current market conditions. If all the assumed discount rates would change by 10%, the fair value of the loan portfolio would change by LVL 8.6 million.

Held to maturity securities

Held to maturity securities are valued using unadjusted quoted prices in active markets, where available. In other instances, either quotes of market participants are used or value of securities is determined using valuation models employing observable or non-observable market inputs.

Customer deposits

The fair value of customer deposits repayable on demand is their carrying amount. The fair value of other deposits is calculated by discounting expected cash flows using average market interest rates close to or at year-end. If all the assumed discount rates would change by 10%, the fair value of the deposit portfolio would change by LVL 0.5 million.

Issued debt

The value of issued debt is determined using either valuation models employing observable or non-observable market inputs or quotes of market participants.

Subordinated liabilities

The value of subordinated liabilities approximates the carrying amount.

Fair value hierarchy

Quoted market prices

Financial instruments are valued using unadjusted quoted prices in active markets.

Valuation technique - observable market inputs

Financial instruments are valued using techniques based on observable market data. In some instances, valuations received from independent third party are used.

Valuation technique - non-market observable inputs

Financial instruments are valued using techniques for which significant inputs are not based on observable market data.

The following table presents fair values of Group's financial assets and liabilities as at 31 December 2010.

	Carrying value	Adjustment to (arrive at) fair value	Fair value		
			Quoted market prices	Valuation technique - observable market inputs	Valuation technique - non-market observable inputs
Cash and demand deposits with central banks	187,220	-	-	187,220	-
Balances due from credit institution	219,624	-	-	219,624	-
Held-for-trading securities	174	-	174	-	-
Financial assets designated at fair value through profit or loss	3,318	-	3,318	-	-
Derivatives	2,670	-	-	2,670	-
Available-for-sale securities	196,991	-	196,991	-	-
Loans and receivables to customers	794,329	(23,674)	-	-	770,655
Held to maturity securities	127,572	2,635	121,358	8,849	-
Total financial assets	1,531,898	(21,039)	321,841	418,363	770,655
Derivatives	644	-	-	644	-
Financial liabilities designated at fair value through profit or loss	1,484	-	1,484	-	-
<i>Financial liabilities measured at amortised cost:</i>					
Balances due to credit institutions and central banks	70,559	-	-	70,559	-
Customer deposits	1,294,335	(5,252)	-	56,204	1,232,879
Issued debt	91,485	(134)	-	-	91,351
Subordinated liabilities	51,235	-	-	-	51,235
Other financial liabilities	7,333	1,714	-	-	9,047
Total financial liabilities	1,517,075	(3,672)	1,484	127,407	1,384,512

The following table presents fair values of Bank's financial assets and liabilities as at 31 December 2010.

	Carrying value	Adjustment to (arrive at) fair value	Fair value		
			Quoted market prices	Valuation technique - observable market inputs	Valuation technique - non-market observable inputs
Cash and demand deposits with central banks	177,348	-	-	177,348	-
Balances due from credit institution	211,608	-	-	211,608	-
Held-for-trading securities	4	-	4	-	-
Derivatives	2,716	-	-	2,716	-
Available-for-sale securities	152,927	-	152,927	-	-
Loans and receivables to customers	691,098	(23,355)	-	-	667,743
Held to maturity securities	117,280	1,872	119,152	-	-
Total financial assets	1,352,981	(21,483)	272,083	391,672	667,743
Derivatives	702	-	-	702	-
<i>Financial liabilities measured at amortised cost:</i>					
Balances due to credit institutions and central banks	82,175	-	-	82,175	-
Customer deposits	1,117,274	(5,923)	-	-	1,111,351
Issued debt	91,557	(134)	-	-	91,423
Subordinated liabilities	51,235	-	-	-	51,235
Total financial liabilities	1,342,943	(6,057)	-	82,877	1,254,009

e) Currency risk

Currency risk is a risk of loss arising from fluctuations in currency exchange rates.

Currency risk management in the Group is carried out in accordance with the Group's Currency Risk Management Policy. Currency risk is assessed and decisions on limits set are made by the Financial Market and Counterparty Committee (FMCC). The decisions of FMCC are approved by the Bank's Management Board. FMCC defines the acceptable currency risk level and the Group's internal limit system, as well as monitors compliance with these limits.

Day-to-day currency risk management is the responsibility of Treasury Sector, while risk monitoring and reporting is the responsibility of Risk and Compliance Sector. The Group has set a limit for open currency positions in each currency at 10% of its equity, and the limit for the total open currency position at 20% of its equity. The limits are equal to the requirements by Latvian legislation. To manage the currency risk, the Group and Bank derivative financial instruments. To assess currency risk, the Group uses scenario analysis. In the event of exchange rates for the following currencies in which the Group and the Bank has open positions adversely change as per scenario below, the potential total decrease in the Group's and Bank's 6 month pre-tax profit would amount to approximately:

Scenario:	Bank LVL 000's				Group LVL 000's			
	USD	CHF	RUR	Total for all currencies	USD	CHF	RUR	Total for all currencies
2% adverse change	80	2	2	369	49	232	3	1,702
5% adverse change	199	6	6	923	122	581	7	4,254

In 2010 the Bank was in compliance with currency position limits.

The following table provides an analysis of the Group's and Bank's assets and liabilities and shareholders' equity as well as memorandum items outstanding as at 31 December 2010 and 2008 by currency profile:

	Group as at 31/12/2010, LVL 000's								
	LVL	USD	EUR	CHF	EEK	LTL	RUB	Other	Total
Assets									
Cash and deposits with central banks	126,322	4,633	12,521	2,303	31,624	6,691	470	2,656	187,220
Balances due from credit institutions	13,274	67,881	129,500	708	101	144	4,620	3,396	219,624
Securities held for trading	-	-	106	-	-	-	68	-	174
Financial assets designated at fair value through profit or loss	137	373	2,808	-	-	-	-	-	3,318
Available-for-sale securities	56,876	26,184	94,779	8,073	-	7,861	-	3,218	196,991
Loans and receivables to customers	64,711	138,058	526,751	3,933	18,381	41,428	877	190	794,329
Held-to-maturity securities	117,280	6,545	3,747	-	-	-	-	-	127,572
Derivatives financial instruments	2,585	18	42	-	-	25	-	-	2,670
Other assets	72,413	179	1,076	105	482	5,505	95	756	80,611
Total assets	453,598	243,871	771,330	15,122	50,588	61,654	6,130	10,216	1,612,509
Liabilities									
Financial liabilities designated at fair value through profit or loss	566	226	692	-	-	-	-	-	1,484
Financial liabilities measured at amortised cost	283,522	293,406	739,998	4,477	50,184	71,471	17,650	54,239	1,514,947
Derivative financial instruments	606	-	26	-	-	12	-	-	644
Other liabilities	8,463	1,253	1,212	1,012	119	997	99	252	13,407
Total liabilities	293,157	294,885	741,928	5,489	50,303	72,480	17,749	54,491	1,530,482
Equity	82,027	-	-	-	-	-	-	-	82,027
Total liabilities and equity	375,184	294,885	741,928	5,489	50,303	72,480	17,749	54,491	1,612,509
Net long/ (short) position for balance sheet items	78,414	(51,014)	29,402	9,633	285	(10,826)	(11,619)	(44,275)	-
Off-balance sheet claims arising from foreign exchange									
Spot exchange contracts	-	2,573	(9,517)	40	-	10,864	(4,216)	227	(29)
Forward foreign exchange contracts	4,255	4,836	(9,316)	274	-	-	4	-	53
Swap exchange contracts	(89,500)	41,167	(46,146)	1,674	4,546	25,243	15,964	49,013	1,961
Net long/ (short) positions on foreign exchange	(85,245)	48,576	(64,979)	1,988	4,546	36,107	11,752	49,240	1,985
Net long/ (short) position as at 31 December 2010	(6,831)	(2,438)	(35,577)	11,621	4,831	25,281	133	4,965	1,985
Exchange rates applied as at 31 December 2010 (LVL for 1 foreign currency unit)									
	-	0.535	0.702804	0.563	0.0449	0.203	0.0176	-	-

	Bank as at 31/12/2010, LVL 000's								
	LVL	USD	EUR	CHF	EEK	LTL	RUB	Other	Total
Assets									
Cash and deposits with central banks	126,313	4,131	11,848	407	31,624	144	417	2,464	177,348
Balances due from credit institutions	12,456	52,559	136,134	200	87	4,083	4,545	1,544	211,608
Securities held for trading	-	-	4	-	-	-	-	-	4
Available-for-sale securities	56,876	12,065	80,792	-	-	-	-	3,194	152,927
Loans and receivables to customers	64,594	131,283	474,611	3,933	15,555	-	877	245	691,098
Held-to-maturity securities	117,280	-	-	-	-	-	-	-	117,280
Derivatives financial instruments	2,656	18	42	-	-	-	-	-	2,716
Other assets	81,637	119	688	13	29	2	19	414	82,921
Total assets	461,812	200,175	704,119	4,553	47,295	4,229	5,858	7,861	1,435,902
Liabilities									
Financial liabilities measured at amortised cost	285,573	242,135	687,193	6,369	51,043	116	17,391	52,421	1,342,241
Derivative financial instruments	676	-	26	-	-	-	-	-	702
Other liabilities	6,885	1,086	527	3	75	3	90	250	8,919
Total liabilities	293,134	243,221	687,746	6,372	51,118	119	17,481	52,671	1,351,862
Equity	84,040	-	-	-	-	-	-	-	84,040
Total liabilities and equity	377,174	243,221	687,746	6,372	51,118	119	17,481	52,671	1,435,902
Net long/ (short) position for balance sheet items	84,638	(43,046)	16,373	(1,819)	(3,823)	4,110	(11,623)	(44,810)	-
Off-balance sheet claims arising from foreign exchange									
Spot exchange contracts	-	2,104	1,802	40	-	-	(4,216)	236	(34)
Forward foreign exchange contracts	4,255	5,304	14,815	274	-	(24,532)	4	-	120
Swap exchange contracts	(89,500)	31,662	(36,357)	1,618	4,546	25,243	15,718	48,958	1,888
Net long/ (short) positions on foreign exchange	(85,245)	39,070	(19,740)	1,932	4,546	711	11,506	49,194	1,974
Net long/ (short) position as at 31 December 2010	(607)	(3,976)	(3,367)	113	723	4,821	(117)	4,384	1,974
Exchange rates applied as at 31 December 2010 (LVL for 1 foreign currency unit)									
	-	0.535	0.702804	0.563	0.0449	0.203	0.0176	-	-

f) *Liquidity risk*

Liquidity risk is the risk that the Group will be unable to meet its legal payment obligations. The purpose of liquidity risk management is to ensure the availability of liquid assets sufficient to meet potential obligations.

The Group manages its liquidity risk in accordance with the Group's Liquidity Risk Management Policy. Liquidity risk is assessed and decisions are made by ALCO. The decisions of ALCO are approved by the Bank's Executive Board. ALCO sets the acceptable liquidity risk level, the Group's internal limit system and defines instruments for the management of liquidity risk, as well as monitors the compliance with the set limits. Daily liquidity management, as well as control is ensured by the Treasury department. Liquidity risk management and reporting in the Group is coordinated by the Risk and Compliance Sector.

The Bank evaluates liquidity risk by using scenario analysis. For this purpose several scenarios of Bank's operations under a variety of conditions are developed: gentle crisis (base case scenario), bank's crisis, general market crisis and a combined scenario. The Bank evaluates its liquidity position for each of the scenarios for variety of periods (ranging from 1 to 3 months). In the Bank a liquidity risk limit and early warning indicator system has been implemented. In addition to scenarios analysis, the Bank also prepares yearly cash flows, which heed assumptions about the most likely flows of funds. For general assessment of asset and liability gaps the Bank regularly prepares and analyses liquidity term structure.

In 2010 the Bank was in compliance with liquidity ratio requirements and mandatory reserve requirements in the Bank of Latvia.

The following table contains Bank's liquidity ratios calculated in accordance with FCMC requirements:

<i>Year</i>	<i>High</i>	<i>Low</i>	<i>Average</i>	<i>Year-end</i>
2010	88%	76%	81%	80%

Liquidity ratio is calculated as liquid assets divided by all liabilities with remaining contractual maturity of 30 days or less. Liquid assets for the purpose of the calculation are cash, balances due from Bank of Latvia and solvent credit institutions placed on demand and up to 30 days and balances redeemable before maturity with insignificant contractual penalties and investments in securities that can be sold in short time or pledged to obtain a loan.

Group's assets, liabilities and memorandum items by contractual maturity structure as at 31 December 2010

	Group as at 31/12/2010, LVL 000's						Total
	Within 1 month	1-3 months	3-6 months	6-12 months	1-5 years	Over 5 years and undated	
Assets							
Cash and deposits with central banks	179,233	-	-	-	-	7,987	187,220
Balances due from credit institutions	199,078	6,800	246	201	13,034	265	219,624
Securities held for trading	34	-	-	-	136	4	174
Financial assets designated at fair value through profit or loss	-	-	-	-	1,483	1,835	3,318
Available-for-sale securities	5,228	10,830	43,891	59,901	54,267	22,874	196,991
Loans and receivables to customers	30,428	14,501	31,329	32,444	408,853	276,774	794,329
Held-to-maturity securities	-	1,374	180	4,288	111,947	9,783	127,572
Derivatives financial instruments	2,618	14	36	2	-	-	2,670
Other assets	5,099	391	2,283	207	141	72,490	80,611
Total assets	421,718	33,910	77,965	97,043	589,861	392,012	1,612,509
Liabilities							
Financial liabilities designated at fair value through profit or loss	-	-	-	-	1,484	-	1,484
Financial liabilities measured at amortised cost	749,926	170,607	212,482	152,730	174,219	54,983	1,514,947
Derivative financial instruments	627	13	-	4	-	-	644
Other liabilities	10,859	625	134	19	667	1,103	13,407
Total liabilities	761,412	171,245	212,616	152,753	176,370	56,086	1,530,482
Equity	-	-	-	-	-	82,027	82,027
Total liabilities and equity	761,412	171,245	212,616	152,753	176,370	138,113	1,612,509
Net balance sheet position – long/ (short)	(339,694)	(137,335)	(134,651)	(55,710)	413,491	253,899	-
Memorandum items							
Contingent liabilities	10,128	-	-	-	-	-	10,128
Financial commitments	91,633	-	-	-	-	-	91,633

Group's contractual undiscounted cash flows of the financial liabilities as at 31 December 2010

The following table represents the analysis of the estimated contractual cash flows arising from Group's financial liabilities as at 31 December 2010:

	LVL 000's						Total contractual cash flows
	Within 1 month	1-3 months	3-6 months	6-12 months	1-5 years	Over 5 years	
Financial liabilities designated at fair value through profit or loss	-	-	-	-	1,484	-	1,484
Financial liabilities measured at amortised cost	750,127	173,710	217,863	158,255	205,984	61,473	1,567,412
Memorandum items							
Contingent liabilities	10,128	-	-	-	-	-	10,128
Financial commitments	91,633	-	-	-	-	-	91,633

Bank's assets, liabilities and memorandum items by contractual maturity structure as at 31 December 2010

	Bank as at 31/12/2010, LVL 000's						Total
	Within 1 month	1-3 months	3-6 months	6-12 months	1-5 years	Over 5 years and undated	
Assets							
Cash and deposits with central banks	177,348	-	-	-	-	-	177,348
Balances due from credit institutions	186,432	12,720	-	-	12,456	-	211,608
Securities held for trading	-	-	-	-	4	-	4
Available-for-sale securities	3,653	8,900	39,142	50,883	28,879	21,470	152,927
Loans and receivables to customers	23,950	46,157	27,825	22,593	352,909	217,664	691,098
Held-to-maturity securities	-	-	-	-	108,103	9,177	117,280
Derivatives financial instruments	2,684	8	22	2	-	-	2,716
Other assets	3,826	10	36	50	14	78,985	82,921
Total assets	397,893	67,795	67,025	73,528	502,365	327,296	1,435,902
Liabilities							
Financial liabilities measured at amortised cost	637,792	154,215	191,820	138,317	168,432	51,665	1,342,241
Derivative financial instruments	693	6	-	3	-	-	702
Other liabilities	8,919	-	-	-	-	-	8,919
Total liabilities	647,404	154,221	191,820	138,320	168,432	51,665	1,351,862
Equity	-	-	-	-	-	84,040	84,040
Total liabilities and equity	647,404	154,221	191,820	138,320	168,432	135,705	1,435,902
Net balance sheet position – long/ (short)	(249,511)	(86,426)	(124,795)	(64,792)	333,933	191,591	-
Memorandum items							
Contingent liabilities	6,724	-	-	-	-	-	6,724
Financial commitments	113,049	-	-	-	-	-	113,049

Banks's contractual undiscounted cash flows of the financial liabilities as at 31 December 2010

	LVL 000's						Total contractual cash flows
	Within 1 month	1-3 months	3-6 months	6-12 months	1-5 years	Over 5 years	
Financial liabilities measured at amortised cost	637,792	156,781	196,744	143,246	199,521	57,832	1,391,916
Memorandum items							
Contingent liabilities	6,724	-	-	-	-	-	6,724
Financial commitments	113,049	-	-	-	-	-	113,049

Group's derivative financial liabilities settled on a net basis and contractual undiscounted cash flows arising from Group's derivatives settled on a gross basis as at 31 December 2010.

	LVL 000's						Total
	Within 1 month	1-3 months	3-6 months	6-12 months	1-5 years	Over 5 years	
Derivatives settled on a net basis							
Foreign exchange contracts	(606)	(6)	-	(3)	-	-	(615)
Interest rate derivatives	-	(5)	(1)	-	-	-	(6)
Derivatives settled on a gross basis							
Foreign exchange derivatives:							
outflow	(4,488)	-	-	(1)	-	-	(4,489)
inflow	4,528	-	-	1	-	-	4,529
Other derivatives:							
outflow	-	-	-	-	(20)	-	(20)
inflow	-	-	-	-	42	-	42

Bank's derivative financial liabilities settled on a net basis and contractual undiscounted cash flows arising from Bank's derivatives settled on a gross basis as at 31 December 2010.

	LVL 000's						Total
	Within 1 month	1-3 months	3-6 months	6-12 months	1-5 years	Over 5 years	
Derivatives settled on a net basis							
Foreign exchange contracts	(664)	(6)	-	(3)	-	-	(673)
Interest rate derivatives	-	(5)	(1)	-	-	-	(6)
Derivatives settled on a gross basis							
Foreign exchange derivatives:							
outflow	(4,697)	-	-	-	-	-	(4,697)
inflow	4,734	-	-	-	-	-	4,734
Other derivatives:							
outflow	-	-	-	-	(20)	-	(20)
inflow	-	-	-	-	42	-	42

g) Operational risk

The Group defines operational risk as the risk of losses resulting from processes that are deficient or non-compliant with requirements of external and internal regulations, losses resulting from actions of employees and system malfunctioning, as well as losses resulting from actions of third parties or from other external conditions, including legal risk (risk of penalty fees, sanctions applied by external institutions, losses resulting from litigation and other similar events), but excluding strategic risk and reputation risk. The Group further divides operational risk into the following categories: personnel risk, process risk, IT and systems risk, external risk.

The Group does not accept operational risks with potential impact exceeding 10% of the Group's net annual revenues, as well as unmanageable risks or risks with unquantifiable impact, irrespective of the financial gains this could bring (i.e., the Group does not perform business activities incurring such operational risks).

The Group applies following approaches for operational risk management:

- Self-assessment of operational risk – the business-owners of the products and processes perform identification and evaluation of potential operational risk events, assessment of the existing control systems and the analysis of the required risk mitigation measures using self-assessment questionnaires and brainstorming sessions with the experts of the respective process;
- Defining operational risk indicators – use of statistical, financial and other indicators that reflect the level of various operational risk types and its changes within the Group;
- Defining the limits of the acceptable losses;
- Operational risk measurement by recording and analysing operational risk events, the extent of the respective damage incurred, causes and other related information (data base of operational risk losses and incidents);
- "Four-eye-principle" and segregation of duties;
- Business continuity planning;
- Risk assessment within product development;
- Insurance;
- Investments in appropriate data processing and information protection technologies.

h) Capital management

Capital adequacy refers to the sufficiency of the Group's capital resources to cover the credit risks and market risks arising from the portfolio of assets and the off-balance sheet exposures. The Financial and Capital Markets Commission's (FCMC), the banking regulator, regulations require Latvian banks to maintain a capital adequacy ratio based on financial statements prepared under IFRS as adopted by EU of 8% of risk weighted assets.

Since the Bank has subsidiaries, which are financial institutions, it should comply with the regulatory requirements based on both the Group's financial statements and the Bank's financial statements as a stand-alone entity.

The Capital Requirements Directive (CRD), which implements Basel II capital regulations in the EU, came into full force on 1 January 2008. In Latvia the directive was implemented through FCMC regulations. Among the options provided in the regulations, the Bank and Group has chosen to use standardized approach in credit risk calculations and basic indicators approach in calculating operation risk charge.

The eligible capital for the capital adequacy purposes constitutes the capital that the Bank manages. The eligible capital comprises of Tier 1 and Tier 2 items, reduced by specific capital charges in accordance with the regulatory requirements.

The capital adequacy calculation of Bank and Group in accordance with FCMC regulations (*Basel II* framework) can be disclosed as follows:

	LVL 000's	
	31/12/2010 Group	31/12/2010 Bank
<i>Tier 1</i>		
- paid-in share capital	103,000	103,000
- audited retained earnings/ (accumulated loss) (not subject to dividend distribution)*	(18,807)	(19,427)
<i>Less</i>		
- intangible assets	(2,001)	(1,256)
- restructuring reserve	(3,389)	-
- Investments in subsidiaries – insurance company (50% from total)*	(1,500)	-
Total Tier 1	77,303	82,317
<i>Tier 2</i>		
- subordinated debt – total	50,270	50,270
- positive securities fair value revaluation reserve	553	467
- Tier 2 excess over 50% from Tier 1	(11,422)	(9,579)
- investments in subsidiaries – insurance company (50% from total)*	(1,500)	-
Total Tier 2	37,901	41,158
Equity to be utilised in the capital adequacy ratio	115,204	123,475
<i>Credit risk and counterparty risk capital charge by regulatory asset classes:</i>		
Central governments and banks	443	57
Municipalities	184	125
Government institutions	19	19
Credit institutions	7,388	8,826
Companies	33,593	34,865
Assets qualifying for "retail" definition	6,651	4,431
Qualifying residential mortgage loans	8,211	5,989
Assets qualifying for "past due" definition	3,017	2,655
Covered bonds	113	113
Investment funds	750	750
Other assets	16,137	10,948
<i>Other risk capital charges:</i>		
Foreign currency open positions subject to capital charge	3,756	635
Fixed income securities position risk capital charge	168	168
Equity instruments' position risk capital charge	-	-
Operational risk capital charge	11,604	9,390
Total capital charges	92,034	78,971
Capital Adequacy Ratio (Equity/Total capital charges) x 8%	10.0%	12.5%

* AAS Citadele Life is not included in consolidation group for capital adequacy purposes. The investment value directly reduces the equity eligible for the capital adequacy ratio calculation purposes.

NOTE 36. EVENTS AFTER THE BALANCE SHEET DATE

Early repayment of Ministry of Finance deposit

On 18 January 2011 the Bank repaid EUR 46.6 million to Ministry of Finance, half a year ahead of the schedule.

Changes in subordinated debt agreements with State JSC Privatisation Agency

On 31 January 2011, the Bank and *JSC Privatisation Agency* agreed to amend the subordinated debt agreement concluded on 22 May 2009, whereby the mechanism for subordinated rate determination was changed. Effective from 1 January 2011 until 7 February 2011, the interest rate was changed from 20.861% to 8.84% and as of 8 February 2011 it is 8.8%. From then on, the rate will be revised on semi-annual basis.

Ministry of Finance deposit interest rate change

Based on the deposit agreements concluded with Ministry of Finance in relation to the State aid received by the Bank, as of 1 January 2011, the interest rate on the deposits received from the Ministry of Finance was revised from 10.003% p.a. to 5.01%. The rate is revised on a quarterly basis.

Agreement with AS Parex Banka

On 19 April 2011, the Bank concluded agreement with AS Parex Banka, whereby both parties agreed to adjust the initial price established, when concluding share purchase agreement on buying AB Citadele Bankas (Lithuania) shares in 2010. For more information please refer to Note 18.

Competition council's decision

On 3 March 2011, the Competition council took the decision to fine 22 Latvian commercial banks for allegedly fixing commission fees for ATM and credit card payments. The Competition council's calculated fine for the Bank amounted to LVL 1.2 million. The Bank disagrees with the decision and will appeal.



Translation from Latvian original*

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of AS Citadele banka

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of AS Citadele banka and its subsidiaries (the "Group") and financial statements of AS Citadele banka (the "Bank") on pages 8 to 68, which comprise the balance sheets as of 31 December 2010 and the statements of income and the statements of comprehensive income, changes in equity and cash flows for the 6 month period ended 31 December 2010 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.

*PricewaterhouseCoopers SIA, Kr. Valdemara iela 19, Riga LV-1010, Latvia
T: +371 6709 4400, F: +371 6783 0055, www.pwc.lv*

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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 Group and the Bank as of 31 December 2010, and of its financial performance and its cash flows for the 6 month period 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 5 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

A blue ink signature of Ahmed Abu Sharkh, consisting of several overlapping loops and a long horizontal stroke.

Ahmed Abu Sharkh
Chairman of the Board

A blue ink signature of Ilandra Lejiņa, written in a cursive style.

Ilandra Lejiņa
Certified auditor in charge
Certificate No. 168

Riga, Latvia
16 May 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.