BANK M2M EUROPE AS

(formerly Latvijas Biznesa banka AS)

2013 Annual Report

Content

MANAGEMENT REPORT ON THE GROUP AND THE BANK'S OPERATIONS DURING 2013

The year of 2013 was a year of major changes at Bank M2M Europe AS ("Bank"). Following the change of shareholders, we have launched a new bank – with a new brand name, strategy, Board of directors and Management team. The range of services offered by the Bank was tailored according to the new strategy, which encompasses providing private banking services to high net worth individuals and the servicing of their business's needs. After the acquisition of 100% shares of investment company M2M Asset Management IPAS, the Bank started offering discretionary portfolio management services in addition to traditional banking products.

Clients of Bank M2M Europe AS are high net worth individuals with investable assets exceeding LVL 700 thousand. We strive to provide the best specifically customized service for each of our clients. By fully understanding the needs of our clients we can offer the best personalized solutions for each case that may arise. We know how to cater to the high and growing expectations of our clients. Bank M2M Europe AS is a transparent and predictable partner both in decision making and customer service. That nowadays is one of the most important aspects when choosing the best bank for the servicing one's financial needs.

Bank M2M Europe AS has made significant investments in 2013. The Bank's share capital was increased by LVL 7 million. We have invested in the improvement of IT infrastructure, IT systems, as well as in the development of the product range. We have put together a new team of highly qualified professionals. These investments were vital to be able to offer the level of service that meets the highest requirements of our clients. Losses of 2013 are related to these investments. Management suggests that the Bank's equity capital be used to cover the losses .

In the last quarter of 2013, after the launch of operation at full scale, the number of clients, as well as the amount of deposits in the Bank, has substantially increased. At the end of the year 2013, the Bank's assets stood at LVL 25mln (an increase of LVL 21mln year on year), shareholder's equity – LVL 9mln (a LVL 5mln year on year increase), deposits – LVL 15mln (a LVL 15mln year on year increase), assets under management (including funds at M2M Asset Management IPAS) – LVL 44mln (2012: LVL 39mln)[1] .

To achieve our main principle – to be a reliable bank, we devote a lot of attention to risk management. The Bank's capital adequacy and liquidity ratios were significantly above the minimum levels set by the regulator: 57.44% and 196% respectively. As of year end, the Bank's assets primarily consist of balances at our correspondent bank accounts and a portfolio of liquid bonds, while the credit portfolio comprises 13% of the Bank's assets. Last year, the Bank has significantly improved its operational risk management system and has strengthened security of confidential information.

The Management of Bank M2M Europe is satisfied of what has been achieved in year 2013, which will serve as the basis for the planned growth of business in 2014. We will continue to implement long-term strategy of shareholders to become the leading private banking service provider in the Baltic region.

[1] Assets under management of M2M Asset Management IPAS at the end of 2012 prior acquisition by the Bank.

In 2014 we will continue to expand the range of products. At the start of the year we will launch a new product – "M2M Supreme". This package of services will introduce a variety of new and innovative features previously unavailable in the local market, it will also enable a more productive and efficient collaboration between the Bank and its clients. We are aware of the latest technological advancements and their growing role in everyday life, thus one of our top priorities in 2014 will be to upgrade and boost the functionality of our internet bank to make it more user-friendly and equally easy to use from both stationary and mobile devices.

The Bank's management team would like to thank the clients for trusting Bank M2M Europe AS in its initial operational phase. We have become a reliable financial service provider and advisor for many of you and are committed to strengthen our mutual business in the future.

The Bank's management would like to express gratitude to the shareholder of Bank M2M Europe AS for support in strengthening the capital base and strategic management of the Bank. And last, but not least, we would like to thank every employee of Bank M2M Europe AS for the professional development of the product range and, essentially, establishing a brand new bank in such a short time frame.

On behalf of the management:

Andrey Vdovin
Chairman of the Council

Roberts Idelsons
Chairman of the Board

19 February 2014

The Council and Management of the Bank

Supervisory Council of the Bank

Position	Name	Last election date	Resignation date
Chairman of the Supervisory Council	Andrey Vdovin	31.05.2013	-
Deputy Chairman of the Supervisory Council	Peter Charles Percival Hambro	31.05.2013	-
Member of the Supervisory Council	Thomas Roland Evert Neckmar	31.05.2013	-
Chairman of the Supervisory Council	Jakovs Šurs	19.06.2012	21.05.2013
Member of the Supervisory Council	Ainis Dābols	19.06.2012	21.05.2013
Member of the Supervisory Council	Sergejs Magins	19.06.2012	21.05.2013
Member of the Supervisory Council	Marija Gribanova	19.06.2012	21.05.2013

Management Board of the Bank

Position	Name	Last election date	Resignation date
Chairman of the Management Board	Roberts Idelsons	15.06.2013	-
Member of the Management Board	Sergejs Zaicevs	20.06.2013	-
Member of the Management Board	Tatjana Drobina	20.06.2013	-
Chairman of the Management Board	Inesis Feiferis	15.05.2012	14.06.2013
Member of the Management Board	Nelli Sorokina	28.09.2012	24.04.2013
Member of the Management Board	Jānis Solovjakovs	26.08.2012	20.06.2013

Report of Responsibility of the Management

The management of Bank M2M Europe AS (the Bank) is responsible for the preparation of the financial statements of the Bank and its subsidiaries (the Group) that reflect the Bank and the Group's financial position at the end of the reported period in a clear and actual manner, as well as for the financial results and the movement of monetary assets during the reported period.

The Bank's management confirms that throughout the preparation of pages 9 to 70 of the financial statements of the Bank and the Group for 2013 the corresponding bookkeeping methods have been used consistently, and that the decisions and evaluations of the Bank's management during the preparation of the financial statement have been in all respects sufficient, well-considered and balanced.

The Bank's management confirms, that International Financial Reporting Standards as adopted by the European Union have been observed in all respects, and that the financial statements have been prepared in accordance with, and correspond to Regulations on the Preparation of An Annual Statement and A Consolidated Annual Statement for Credit Institutions, Investment Brokerage Companies and Investment Management Companies approved by the Financial and Capital Market Commission of the Republic of Latvia.

The Bank's management is responsible for the maintenance of the corresponding bookkeeping system, preservation of the Bank's assets, as well as for the exposure and prevention of fraud and other violations of law.

The Bank's management is also responsible for the observation of requirements of the Law on Credit Institutions, other legislative acts of the Republic of Latvia, as well as for the observation of the regulations of the Bank of Latvia and the Financial and Capital Market Commission.

On behalf of the management:

Andrey Vdovin
Chairman of the Council

Roberts Idelsons
Chairman of the Board

19 February 2014

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Independent Auditors' Report

To the shareholder of AS "Bank M2M Europe"

Report on the Separate and Consolidated Financial Statements

We have audited the accompanying separate financial statements of AS "Bank M2M Europe" ("the Bank"), which comprise the separate statement of financial position as at 31 December 2013, the separate statement of profit or loss, changes in shareholders' equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages 9 to 70. We have also audited the accompanying consolidated financial statements of AS "Bank M2M Europe" and its subsidiary ("the Group"), which comprise the consolidated statement of financial position as at 31 December 2013, the consolidated statement of profit or loss, changes in shareholders' equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages 9 to 70.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these separate and consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the European Union and for such internal controls as management determines are necessary to enable the preparation of these financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the separate and consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of these financial statements, whether due to fraud or error. In making those risk assessments, we consider internal controls relevant to the Bank's and Group's preparation and fair presentation of these 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 Bank's and Group's internal controls. An audit also includes evaluating the appropriateness of accounting principles used and the reasonableness of accounting estimates made by Bank's and Group's management, as well as evaluating the overall presentation of the separate and consolidated financial statements.

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

Opinion

In our opinion, the separate financial statements give a true and fair view of the financial position of the AS "Bank M2M Europe" as at 31 December 2013, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the AS "Bank M2M Europe" and its subsidiary as at 31 December 2013, and of the consolidated financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

Other matters

The comparative information of the prior periods disclosed in the Bank's financial statements is based on the financial statements of the Bank as at and for the year ended 31 December 2012 which were audited by another auditor who expressed an unmodified opinion on those statements on 14 March 2013.

Report on Other Legal and Regulatory Requirements

In addition, our responsibility is to assess whether the accounting information included in the Management Report, as set out on pages 3 to 4, the preparation of which is the responsibility of management, is consistent with the separate and consolidated financial statements. Our work with respect to the Management Report was limited to the aforementioned scope and did not include a review of any information other than drawn from the financial statements. In our opinion, financial information included in the Management Report is consistent with the information in the separate and consolidated financial statements.

KPMG Baltics SIA
License No 55

Ondrej Fikrle
Partner pp KPMG Baltics SIA
Riga, Latvia
19 February 2014

Inga Lipšāne
Sworn Auditor
Certificate No 112

GROUP'S CONSOLIDATED AND BANK'S SEPARATE STATEMENT OF LOSS

For the year ended 31 December 2013 **'000 LVL**	**Note**	**2013 Group**	**2013 Bank**	**2012 Bank**
Interest income	7	113	112	4
Interest expense	7	(39)	(39)	(5)
Net interest income		**74**	**73**	**(1)**
Fee and commission income	8	122	85	38
Fee and commission expense	9	(60)	(58)	(13)
Net fee and commission income		**62**	**27**	**25**
Net gain/(loss) on financial assets at fair value through profit or loss	10	(14)	(14)	-
Net foreign exchange income/(loss)	11	25	25	(4)
Net realised gain/(loss) on Available-for-sale financial assets	12	16	16	-
Other income	13	29	29	109
Total operating income		**192**	**156**	**129**
General administrative expenses	14	(2 207)	(2 173)	(1 930)
Other expenses	15	-	-	(96)
Impairment loss	16	(49)	(49)	-
Loss before income tax		**(2 064)**	**(2 066)**	**(1 897)**
Income tax benefit	17	21	21	2
Loss for the period		**(2 043)**	**(2 045)**	**(1 895)**
Items that are or may be reclassified to profit or loss				
Available-for-sale financial assets – net change in fair value		38	38	-
Available for sale financial assets – reclassified to profit or loss		(25)	(25)	-
Other comprehensive income for the period		**13**	**13**	-
Total comprehensive expense		**(2 030)**	**(2 032)**	**(1 895)**

The accompanying notes on pages 16 to 70 are an integral part of these consolidated financial statements.

The consolidated financial statements as set out on pages 9 to 70 were approved by management of the Bank on 19 February 2014.

On behalf of the management:

Andrey Vdovin
Chairman of the Council

Roberts Idelsons
Chairman of the Board

GROUP'S CONSOLIDATED AND BANK'S SEPARATE STATEMENT OF FINANCIAL POSITION

As at 31 December 2013

'000 LVL	**Note**	**2013 Group**	**2013 Bank**	**2012 Bank**
ASSETS				
Cash and due from central banks	18	1 788	1 788	394
Financial assets at fair value through profit or loss	19	110	110	-
Loans and advances due from financial institutions	20	9 106	8 533	1 371
Loans and advances due from customers	21	3 243	3 243	198
Available-for-sale financial assets	22	7 008	7 008	-
Held-to-maturity investments	23	1 199	1 199	-
Investments in subsidiary	24	-	1 317	-
Property and equipment	25	1 318	1 306	1 734
Goodwill and other intangible assets	26	917	363	2
Other assets	27	584	562	537
Total Assets		**25 273**	**25 429**	**4 236**

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Chairman of the Board

GROUP'S CONSOLIDATED AND BANK'S SEPARATE STATEMENT OF FINANCIAL POSITION

As at 31 December 2013

'000 LVL

LIABILITIES AND SHAREHOLDERS' EQUITY	**Note**	**2013 Group**	**2013 Bank**	**2012 Bank**
Financial assets at fair value through profit or loss	19	20	20	-
Current accounts and deposits due to customers	28	14 534	14 709	106
Subordinated debt	29	1 409	1 409	-
Deferred tax liability	30	-	-	21
Provisions	31	89	89	92
Other liabilities	32	187	170	340
Total Liabilities		16 239	16 397	559
Share capital	33	19 622	19 622	12 235
Share premium		20	20	20
Revaluation reserve of available-for-sale financial assets		13	13	-
Other reserves		219	219	219
Accumulated losses		(10 840)	(10 842)	(8 797)
Total Shareholders' Equity		**9 034**	**9 032**	**3 677**
Total Liabilities and Shareholders' Equity		**25 273**	**25 429**	**4 236**
Assets under management	35	**43 530**	**2 360**	-

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On behalf of the management:

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Chairman of the Board

GROUP'S CONSOLIDATED AND BANK'S SEPARATE STATEMENT OF CASH FLOWS	Note			
For the year ended 31 December 2013		**2013 Group ’000 LVL**	**2013 Bank ‘000 LVL**	**2012 Bank ‘000 LVL**
CASH FLOWS FROM OPERATING ACTIVITIES				
Loss before income tax		**(2 064)**	**(2 066)**	**(1 897)**
Amortisation and depreciation	14	181	176	123
Increase of provisions		(3)	(3)	96
Impairment losses		49	49	-
Decrease in cash and cash equivalents before changes in assets and liabilities, as a result of ordinary operations		(1 837)	(1 844)	(1 678)
Decrease in financial assets at fair value through profit or loss		(90)	(90)	-
Increase in loans and advances due from financial institutions		(1 380)	(871)	-
Decrease in loans and advances due from customers		(3 045)	(3 045)	(198)
Decrease in available-for-sale financial assets		(6 995)	(6 995)	-
Decrease in other assets		(93)	(74)	(252)
Increase in deposits and balances due to financial institutions		14 428	14 603	159
Decrease in other liabilities		(153)	(170)	(7)
Increase/(decrease) in cash and cash equivalents from operating activities		**2 672**	**3 358**	**(298)**
CASH FLOW FROM INVESTING ACTIVITIES				
Purchase of property and equipment		(109)	(109)	(38)
Acquisition of subsidiary	39	(574)	(1 317)	-
Purchase of held-to-maturity financial investments		(1 199)	(1 199)	-
Decrease in cash and cash equivalents from investing activities		**(1 882)**	**(2 625)**	**(38)**

CASH FLOW FROM FINANCING ACTIVITIES				
Increase in share capital		7 387	7 387	1 405
Increase in other borrowed funds		1 409	1 409	-
Increase in cash and cash equivalents from financing activities		**8 796**	**8 796**	**1 405**
Net cash flow for the period		**7 749**	**7 685**	**(609)**
Cash and cash equivalents at the beginning of the year		**1 765**	**1 765**	**2 374**
Cash and cash equivalents at the end of the year	18	**9 514**	**9 450**	**1 765**

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On behalf of the management:

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THE GROUP'S CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
For the year ended 31 December 2013

'000 LVL	Share capital	Share premium	Revaluation reserve of available-for-sale financial assets	Other reserves	Accumulated losses	Total
Balance at 1 January 2013	**12 235**	**20**	**-**	**219**	**(8 797)**	**3 677**
Total comprehensive income						
Loss for the period	-	-	-	-	(2 043)	**(2 043)**
Other comprehensive income	-	-	13	-	-	**13**
Transactions with shareholders recorded directly in equity						
Increase of share capital	7 387	-	-	-	-	**7 387**
Balance at 31 December 2013	**19 622**	**20**	**13**	**219**	**(10 840)**	**9 034**

The accompanying notes on pages 16 to 70 are an integral part of these consolidated financial statements.

The consolidated financial statements as set out on pages 9 to 70 were approved by management of the Bank on 19 February 2014.

On behalf of the management:

Andrey Vdovin
Chairman of the Council

Roberts Idelsons
Chairman of the Board

THE BANK'S SEPARATE STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
For the year ended 31 December 2013

'000 LVL	Share capital	Share premium	Revaluation reserve of available-for-sale financial assets	Other reserves	Accumulated losses	Total
Balance at 1 January 2012	10 830	20	-	219	(6 902)	4 167
Total comprehensive income	-					
Loss for the period		-	-	-	(1 895)	**(1 895)**
Transactions with shareholders recorded directly in equity						
Increase of share capital	1 405	-	-	-	-	**1 405**
Balance at 31 December 2012	12 235	20	-	219	(8 797)	3 677
Total comprehensive income	-					
Loss for the period	-	-	-	-	(2 045)	**(2 045)**
Other comprehensive income		-	13	-	-	**13**
Transactions with shareholders recorded directly in equity						
Increase of share capital	7 387	-	-	-	-	**7 387**
Balance at 31 December 2013	19 622	20	13	219	(10 842)	9 032

The accompanying notes on pages 16 to 70 are an integral part of these consolidated financial statements.

The consolidated financial statements as set out on pages 9 to 70 were approved by management of the Bank on 19 February 2014.

On behalf of the management:

Andrey Vdovin
Chairman of the Council

Roberts Idelsons
Chairman of the Board

1 Background

Principal activities

These consolidated financial statements include the financial statements of Bank M2M Europe AS (the "Bank") and its subsidiary M2M Asset Management IPAS (together referred to as the "Group"). Bank M2M Europe AS was founded in 1992 under the name Latvian Business Bank. On 21 May 2013 the Bank was acquired by Andrey Vdovin, a banker and co-owner of VMHY group. Mr. Vdovin is the sole shareholder of Bank M2M Europe AS, he also is the Chairman of the Council of the Bank.

Bank M2M Europe AS is private banking boutique committed to providing top quality financial solutions to the high net worth clients and companies owned by such clients. Main products offered to the clients are: servicing day to day banking transactions of private and business clients, wealth management solutions including portfolio management and investment advisory, premium level payment cards, deposits, servicing fiduciary transactions and escrow accounts, lombard loans. Bank M2M Europe clients are predominantly residents of Russia and other Former Soviet countries. The Bank strives to become the most reliable private banking institution in the Baltics.

The activities of the Group are supervised by the Bank of Latvia and the Financial and Capital Market Commission ("FCMC"). The registered address of the Bank's head office is 3 Antonijas street, Riga LV-1010, Latvia. The majority of the Group's assets and liabilities are located in Latvia, Europe and CIS countries.

As of 31 December 2013, the Group had 51 employees and the Bank had 43 (2012:43) employees.

The principal subsidiary of the Group is as follows:

			Ownership %	
Name	**Country of incorporation**	**Principal Activities**	**2013**	**2012**
„M2M Asset Management" IPAS	Latvia	Financial services	100	-

2 Basis of preparation

Statement of compliance

The accompanying consolidated financial statements have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union ("EU IFRS"), and regulations of the Financial and Capital Market Commission in force as at the reporting date.

These consolidated financial statements were authorized for issue by the management of the Bank on 19 February 2014. These consolidated financial statements may be amended by the shareholder.

Basis of measurement

The consolidated financial statements are prepared on the historical cost basis except for the following:
- financial assets at fair value through profit or loss are stated at fair value;
- available-for-sale assets are stated at fair value;

Functional and Presentation Currency

The Group's consolidated and the Bank's separate financial statements are presented in thousands of lats ('000 LVL), unless stated otherwise. Subsidiary of the Bank operates in the functional currency of LVL.

3 Significant accounting policies

The following significant accounting policies have been applied in the preparation of the consolidated financial statements. The accounting policies have been consistently applied.

Basis of consolidation

Subsidiaries

Subsidiaries are those enterprises controlled by the Group. Control exists when the Group has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control effectively commences until the date that control effectively ceases.

Assets under management

The Group provides assets management services to individuals and institutions. The assets under management are not included neither in the consolidated and nor in the separate statement of financial position.

Transactions eliminated on consolidation

M2M Asset Management investment management entity (the 'Subsidiary') was acquired by the Bank on 11 November 2013, with Subsidiary's shareholder changes registered on the same date. Bank M2M Europe AS became the sole shareholder of the entity which is now a fully integrated subsidiary of the Bank. Detailed information of the entity is available in Note24.

The Bank and its Subsidiary's financial statements are consolidated in the Group financial statements, merging the respective assets, liabilities, income and expense captions. Intra-group balances and transactions, and any unrealised gains arising from intra-group transactions, have been eliminated in the preparation of these consolidated financial statements.

Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Goodwill on acquisition of subsidiaries is included in intangible assets.

Goodwill is allocated to cash-generating units and is stated at cost less impairment losses.

Goodwill is tested for impairment annually or more frequently if events or changes in circumstances indicate that it might be impaired and is carried at cost less accumulated impairment losses. Gains or losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Negative goodwill arising on an acquisition is recognised immediately in profit or loss.

Foreign currency

Transactions in foreign currencies are translated into the respective functional currency of Group companies at the exchange rate at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated into the functional currency at the spot exchange rate at that date. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value in foreign currency are retranslated into the functional currency at the spot exchange rate at the date that the fair value was determined. Foreign currency differences arising on retranslation are recognised in profit or loss, except for differences arising on the retranslation of available-for-sale equity instruments or a financial liability designated as the hedging instrument in a hedge of the net investment in a foreign operation or in a qualifying cash flow hedge, which are recognised in other comprehensive income.

Cash and cash equivalents

Cash and cash equivalents include notes and coins on hand, unrestricted balances held with central banks and highly liquid financial assets with original maturities of less than three months, which are subject to insignificant risk of changes in their fair value, and are used by the Bank and the Group companies in the management of short-term commitments.

Financial instruments

(i) Classification

Financial assets at fair value through profit or loss are financial assets or liabilities that are acquired or incurred principally for the purpose of selling or repurchasing in the near term; or that are part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking; or that are a derivative (except for a derivative that is a designated and effective hedging instrument); or that are upon initial recognition, designated by the entity as at fair value through the profit or loss.

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Group has the positive intention and ability to hold to maturity, and which are not designated at fair value through profit or loss, or available for sale.

Available-for-sale financial assets are those financial assets that are designated as available-for-sale or are not classified as loans and receivables, Held-to-maturity investments or financial assets at fair value through profit or loss.

Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. For the purposes of these financial statements, loans and advances include regular loans, credit card balances, and are accounted for at amortized cost using the effective interest method. Certain expenses, such as legal fees or sales commissions for employees acting as agents or other expenses that are incurred in securing a loan are treated as part of the cost of the transaction.

(ii) Recognition

Financial assets and liabilities are recognised in the statement of financial position when the Group or the Bank becomes a party to the contractual provisions of the instrument. All regular way purchases of financial assets are accounted for at the *settlement* date.

(iii) Measurement

A financial asset or liability is initially measured at its fair value plus, in the case of a financial asset or liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or liability.

Subsequent to initial recognition, financial assets, including derivatives that are assets, are measured at their fair values, without any deduction for transaction costs that may be incurred on sale or other disposal, except for:

- Held-to-maturity investments and loans and receivables that are measured at amortized cost using the effective interest method; and
- investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured which are measured at cost.

All financial liabilities, other than those designated at fair value through profit or loss and financial liabilities that arise when a transfer of a financial asset carried at fair value does not qualify for derecognition, are measured at amortised cost. Amortised cost is calculated using the effective interest rate method. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument.

Fair value measurement principles

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the Group has access at that date. The fair value of a liability reflects its non-performance risk.

When applicable, the Group measures the fair value of an instrument using quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

To measure the fair value of FX swap and forward deals the Group uses market rates for the similar maturity and currencies. Quotes of certain brokers have been used to determine fair value of bonds which do not have active market.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price, i.e., the fair value of the consideration given or received. If the Group determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that used only data from observable inputs, the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is supported wholly by observable market data or the transaction is closed out.

Portfolios of financial assets and financial liabilities that are exposed to market risk and credit risk that are managed by the Group on the basis of the net exposure to either market or credit risk, are measured on the basis of a price that would be received to sell a net long position (or paid to transfer a net short position) for a particular risk exposure. Those portfolio-level adjustments are allocated to the individual assets and liabilities on the basis of the relative risk adjustment of each of the individual instruments in the portfolio.

The Group recognises transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred. For further analysis of basis for fair value see Note 37.

(v) Gains and losses on subsequent measurement

A gain or loss arising from a change in the fair value of a financial asset or liability is recognised as follows:

- a gain or loss on a financial instrument classified as at fair value through profit or loss is recognised in the profit or loss;
- a gain or loss on an available-for-sale financial asset is recognised in other comprehensive income (except for impairment losses and foreign exchange gains and losses on debt financial instruments) until the asset is derecognised, at which time the cumulative gain or loss previously recognised in equity is recognised in the profit or loss. Interest in relation to an available-for-sale financial asset is recognised as earned in the profit or loss calculated using the effective interest method.

For financial assets and liabilities carried at amortised cost, a gain or loss is recognised in the profit or loss when the financial asset or liability is derecognised or impaired, and through the amortization process.

(vi) Derecognition

A financial asset is derecognised when the contractual rights to the cash flows from the financial asset expire or when the Group transfers substantially all of the risks and rewards of ownership of the financial asset. Any rights or obligations created or retained in the transfer are recognised separately as assets or liabilities. A financial liability is derecognised when it is extinguished.

The Group also derecognises certain assets when it writes off balances pertaining to the assets deemed to be uncollectible.

(vii) Repurchase and reverse repurchase agreements

Securities sold under sale and repurchase ("repo") agreements are accounted for as secured financing transactions, with the securities retained in the statement of financial position and the liability towards counterparty included in amounts payable under repo transactions. The difference between the sale and repurchase price represents interest expense and is recognised in the profit or loss over the term of the repo agreement using the effective interest rate method.

Securities purchased under agreements to resell ("reverse repo") are recorded as amounts receivable under reverse repo transactions. The differences between the purchase and resale prices are treated as interest income and accrued over the term of the reverse repo agreement using the effective interest method.

If assets purchased under agreement to resell are sold to third parties, the obligation to return securities is recorded as a trading liability and measured at fair value.

(viii) Derivative financial instruments

Derivative financial instruments include currency swaps and forward contracts.

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. All derivatives are carried as assets when their fair value is positive and as liabilities when their fair value is negative.

Changes in the fair value of derivatives are recognised immediately in the profit or loss.

Derivatives may be embedded in another contractual arrangement (a "host contract"). An embedded derivative is separated from the host contract and it is accounted for as a derivative if, and only if the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract, and a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and the combined instrument is not measured at fair value with changes in fair value recognised in the profit or loss. Derivatives embedded in financial assets or financial liabilities at fair value through profit or loss are not separated.

Although the Group trades in derivative instruments for risk hedging purposes, the Group does not adopt hedge accounting.

(ix) Offsetting

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

Property and equipment

Owned assets

Items of property and equipment are stated at cost less accumulated depreciation and impairment losses, except for buildings which are stated at revalued amounts as described below.

Where an item of property and equipment comprises major components having different useful lives, they are accounted for as separate items of property and equipment.

Leased assets

Leasehold improvements are capitalized, and their depreciation is calculated on a straight-line basis over the remaining lease term. Leasehold renovation costs in relation to improving quality and usability of the building are capitalized. Depreciation of these assets is calculated on a straight-line basis over their useful life.

Leasehold maintenance and current repair costs are recognised in the profit or loss statement when incurred.

Depreciation

Depreciation is charged to the profit or loss on a straight-line basis over the estimated useful lives of the individual assets. Depreciation commences on the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and ready for use. Land is not depreciated. The estimated useful lives are as follows:

Leasehold improvements	Over the lease term
Equipment	3 years
Fixtures and fittings	5 years

Intangible assets

Intangible assets, which are acquired by the Group, are stated at cost less accumulated amortisation and impairment losses.

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software.

Subsequent expenditure on intangible assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates.

Costs associated with maintaining computer software programs are recognised as an expense as incurred.

Amortisation is charged to the profit or loss on a straight-line basis over the estimated useful lives of intangible assets. The estimated useful lives are as follows:

Intangible assets	5 years

Impairment

Financial assets

At each reporting date the Group assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash flows of the asset that can be estimated reliably.

Objective evidence that financial assets (including equity securities) are impaired can include default or delinquency by a borrower, restructuring of a loan or advance by the Group on terms that the Group would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in a group, or economic conditions that correlate with defaults in a group. In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

All held-to-maturity and available for sale investment securities are assessed for specific impairment.

The Group considers evidence of impairment for loans and advances at specific asset level only. Given the level of activity and exposure to assets, the management is confident that collective impairment assessment is not necessary.

Impairment losses on assets carried at amortised cost are measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognised in profit or loss and reflected in an allowance account against loans and advances. Interest on the impaired asset continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

Impairment losses on available-for-sale investment securities are recognised by transferring the cumulative loss that has been recognised in other comprehensive income to profit or loss. The cumulative loss that is removed from equity and recognised in profit or loss is the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less any impairment loss previously recognised in statement of comprehensive income. Changes in impairment provisions attributable to time value are reflected as a component of interest income.

If, in a subsequent period, the fair value of an impaired available-for-sale debt security 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, with the amount of the reversal recognised in profit or loss. However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognised in other comprehensive income.

Non-financial assets

The carrying amounts of the Group's non-financial assets, other than deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets and groups. Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Provisions

A provision is recognised in the statement of financial position when the Group has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

Credit related commitments

In the normal course of business, the Group enters into credit related commitments, and provides guarantees and letters of credit.

Taxation

Income tax expense comprises current and deferred tax. Income tax expense is recognised in the profit or loss except to the extent that it relates to items recognised directly in equity or in other comprehensive income.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of goodwill, the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss, and differences relating to investments in subsidiaries to the extent that they probably will not reverse in the foreseeable future. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Income and expense recognition

With the exception of financial instruments held for trading and other financial assets at fair value through profit or loss, interest income and expense are recognised in the consolidated statement of income using the effective interest rate method. Interest income on financial instruments held for trading and on other financial assets at fair value through profit or loss comprises coupon interest only.

Accrued discounts and premiums on financial assets at fair value through profit or loss are recognised in gains less losses from financial assets at fair value through profit or loss, respectively.

Loan origination fees and other fees that are considered to be integral to the overall profitability of a loan, together with the related direct costs, are deferred and amortized to interest income over the estimated life of the financial instrument using the effective interest rate method.

Other fees, commissions and other income and expense items are recognised when the corresponding service has been provided.

Changes in accounting policies

Except for the changes below, the Group has consistently applied the accounting policies set out in Note 3 to all periods presented in these consolidated financial statements.

The Group has adopted the following new standards and amendments to standards, including any consequential amendments to other standards, with a date of initial application of 1 January 2013.

(i) Fair value measurement

IFRS 13 establishes a single framework for measuring fair value and making disclosure about fair value measurements when such measurements are required or permitted by other IFRSs. It unifies the definition of the fair value as the price that would be received to sell an asset or pad to transfer a liability in an orderly transaction between market participants at the measurement date. It replaces and expands the disclosure requirements about fair value measurements in other IFRSs, including IFRS 7. As a result, the Group has included additional disclosures in this regards (see Note 37 (Fair value of financial instruments)).

In accordance with the transitional provisions of IFRS 13, the Group has applied the new fair value measurement guidance prospectively and has not provided any comparative information for new disclosures. Notwithstanding the above, the change had no significant impact on the measurements of the Group's assets and liabilities.

In accordance with the transitional provisions of IFRS 13, the Group has applied the new fair value measurement guidance prospectively and has not provided any comparative information for new disclosures. Notwithstanding the above, the change had no significant impact on the measurements of the Group's assets and liabilities.

(ii) Presentation of items of Other comprehensive income

As a result of the amendments to IAS 1, the Group has modified the presentation of items in the statement of Other Comprehensive Income, to present separately items that would be reclassified to profit or loss from those that would never be. Comparative information has been re-presented accordingly.

(iii) Other amendments to standards

The following amendments to standards with effective date of 1 January 2013 did not have any impact on these consolidated financial statements:

- Amendment to IFRS 7 – Offsetting of financial assets and liabilities
- Amendment to IAS 19 (2011) – Employee benefits
- Amendments to IAS 12 – Deferred tax: Recovery of Underlying Assets

New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning after 1 January 2013, and have not been applied in preparing these consolidated financial statements. The Group does not plan to adopt these standards early.

<u>IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements, IFRS 12 Disclosure of Interests in Other Entities (2011)</u>

IFRS 10 introduces a single control model to determine whether an investee should be consolidated. As a result, the Group may need to change its consolidation conclusion in respect of its investees, which may lead to changes in the current accounting for these investees. The Group is currently assessing the possible impact on the consolidated financial statements.

Under IFRS 11, the structure of the joint arrangement, although still an important consideration, is no longer the main factor in determining the type of joint arrangement and therefore the subsequent accounting.

- The Group's interest is a joint operation, which is an arrangement in which the parties have rights to the assets and obligations for the liabilities, will be accounted for on the basis of the Group's interest in those assets and liabilities.
- The Group's interest in a joint venture, which is an arrangement in which the parties have rights to the net assets, will be equity-accounted.

The Group does not expect IFRS 11 to have material impact on the financial statements since it is not a party to any joint arrangements.

IFRS 12 brings together into a single standard all the disclosure requirements about an entity's interest in subsidiaries, joint arrangements, associates and unconsolidated structured entities. It is expected that the new Standard, when initially applied, will have a significant impact on the level of disclosure in the financial statements. However, the Group will not prepare an analysis of the impact this will have on the financial statements until the date of initial application.

These standards are effective for annual periods beginning on or after 1 January 2014 with early adoption permitted.

IAS 27 (2011) Separate Financial Statements (effective for annual periods beginning on or after 1 January 2014)

IAS 27 (2011) carries forward the existing accounting and disclosure requirements of IAS 27 (2008) for separate financial statements, with some minor clarifications. As well, the existing requirements of IAS 28 (2008) and IAS 31 for separate financial statements have been incorporated into IAS 27 (2011). The standard no longer addresses the principle of control and requirements relating to the presentation of consolidated financial statements, which have been incorporated into IFRS 10, *Consolidated Financial Statements*. The Group does not expect IAS 27 (2011) to have a material impact on the financial statements, since it does not result in a change in the entity's accounting policy.

IAS 28 (2011) Investments in Associates and Joint Ventures (effective for annual periods beginning on or after 1 January 2014)

There are limited amendments to IAS 28 (2008) which related to associates and joint ventures held for sale and changes in interest held in associates and joint ventures. The entity does not expect the amendments to Standard to have material impact on the financial statements since it does not have any significant investments in associates or joint ventures that will be impacted by the amendments.

Amendments to IAS 32 on Offsetting Financial Assets and Financial Liabilities (effective for annual periods beginning on or after 1 January 2014)

Amendments to IAS 32 (effective for annual periods beginning on or after 1 January 2014; to be applied retrospectively) clarify that an entity currently has a legally enforceable right to set-off if that right is not contingent on a future event and enforceable both in the normal course of business and in the event of default, insolvency or bankruptcy of the entity and all counterparties. The Group does not expect the Amendments to have any impact on the financial statements since the Group does not apply offsetting to any of its financial assets and financial liabilities and have not entered into master netting arrangements.

Amendments to IFRS 10, IFRS 12 and IAS 27 on Investment Entities (effective for annual periods beginning on or after 1 January 2014)

The Amendments provide an exception to the consolidation requirements in IFRS 10 and require qualifying investment entities to measure their investments in controlled entities, as well as investments in associates and joint ventures at fair value through profit or loss, rather than consolidating them. The consolidation exemption is mandatory (i.e. not optional), with the only exception being that subsidiaries that are considered as an extension of the investment entity's investing activities, must still be consolidated. An entity qualifies as an investment entity if it meets all of the essential elements of the definition of an investment entity. The Group does not expect the new standard to have any impact on the financial statements, since the Bank does not qualify as an investment entity.

Amendments to IAS 36 on Recoverable Amount Disclosures for Non-Financial Assets (effective for annual periods beginning on or after 1 January 2014)

The Amendments clarify that recoverable amount should be disclosed only for individual assets (including goodwill) or cash-generated units for which an impairment loss was recognised or reversed during the period. The Amendments also require additional disclosures related to fair value hierarchy when impairment for individual assets (including goodwill) or cash-generated units has been recognised or reversed in the period and recoverable amount is based on fair value less costs to disposal. The amendment does not have any impact on the financial statements, as the Group does not have non-financial assets for which an impairment loss was recognised or reversed during the period.

Amendments to IAS 39 on Novation of Derivatives and Continuation of Hedge Accounting (effective for annual periods beginning on or after 1 January 2014)

The Amendments allows hedge accounting to continue in a situation where a derivative, which has been designated as a hedging instrument, is novated to effect clearing with a central counterparty as a result of laws and regulations, when certain criteria are met. The Group does not expect the new standard to have any impact on the financial statements, since the entity does not apply hedge accounting.

4 Risk management

The Group has exposure to the following risks:

- market risks
- interest rate risk
- currency risk
- price risk
- credit risk
- liquidity risk
- operational risk
- other risks: ML/TF risk (money laundering and terrorism financing risk)risk, compliance and reputation risk, strategic risk

This note presents information about the Bank's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risk.

Risk management policies and procedures

The Group's risk management policies aim to identify, analyse and manage the risks faced by the Group, to set appropriate risk limits and controls, and to continuously monitor risk levels and adherence to limits. Risk management policies and procedures are reviewed regularly to reflect changes in regulation, market conditions, products and services offered and emerging best practice.

The Council has overall responsibility for the oversight of the risk management framework, overseeing the management of key risks and reviewing its risk management policies and procedures as well as approving significantly large exposures.

The Management Board is responsible for monitoring and implementation of risk mitigation measures and making sure that the Group operates within the established risk parameters. The Head of Financial Risk Management Division is responsible for the overall financial risk management functions, ensuring the implementation of common principles and methods for identifying, measuring, managing and reporting financial risks. The Head of Risk and Compliance Department has the same responsibilities in the field of non-financial risks and compliance issues.

Credit, market and liquidity risks both at portfolio and transactional levels are managed and controlled through a system of Credit Committee and Limits Committee For limits over predefined level additional approval from the Council is needed. In order to facilitate efficient decision-making, the Group has established a hierarchy of authorities depending on the type and amount of the exposure.

Market risks

Market risk is the risk that movements in market prices, including foreign exchange rates, interest rates, credit spreads and equity prices will affect the Group's income or the value of its portfolios. Market risks comprise currency risk, interest rate risk and other price risk. Market risk arises from open positions in interest rate, currency and fixed income or other financial instruments, which are exposed to general and specific market movements and changes in the level of volatility of market prices.

The objective of market risk management is to manage and control market risk exposures within acceptable parameters, whilst optimizing the return on risk.

Overall authority for market risk is vested in the Limits Committee (LC), chaired by the CEO. Market risk limits are approved by LC based on recommendations of the Financial Risk Management Division.

The Group manages its market risk by setting open position limits in relation to financial instrument, interest rate maturity and currency positions and stop-loss limits which are monitored on a regular basis and reviewed and approved by the Limits Committee. Additional restrictions are set for financial instrument portfolios, such as duration limits, concentration limits etc.

In addition, the Group uses a wide range of stress tests to model the financial impact of a variety of exceptional market scenarios on individual portfolios and the Group's overall position. Stress tests provide an indication of the potential size of losses that could arise in extreme conditions. The stress tests carried out by the Group include: risk factor stress testing, where stress movements are applied to each risk category and ad hoc stress testing, which includes applying possible stress events to specific positions.

The management of interest rates risk by monitoring interest rate gap is supplemented by monitoring the sensitivity of the Group's net interest margin to various standard and non-standard interest rate scenarios. Sensitivity of net present value of Bank's assets and liabilities is also evaluated.

Interest rate risk

Interest rate risk is the risk that movements in interest rates will affect the Group's income or the value of its portfolios of financial instruments.

The Group is exposed to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest margins may increase as a result of such changes but may also reduce or create losses in the event that unexpected movements arise.

A change of 100 basis points would have increased (decreased) equity and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular foreign exchange rates, remain constant. Only tradable fixed-income financial instruments were evaluated (not including investments in fixed-income funds). Results are the same for the Bank and for the Group because the subsidiary did not have investments in tradable fixed-income financial instruments. The impact of income taxes is not reflected in this analysis:

	31 December 2013		**31 December 2012**	
'000 LVL	**Profit or loss**	**OCI**	**Profit or loss**	**OCI**
100 bp parallel increase	(7)	(186)	-	-
100 bp parallel decrease	7	191	-	-

Currency risk

The Group has assets and liabilities denominated in several foreign currencies. Foreign currency risk arises when the actual or forecasted assets in a foreign currency are either greater or less than the liabilities in that currency. For further information on the Group's exposure to currency risk at year end refer to Currency analysis table in Note 4.

A change in exchange rates as indicated below, as at 31 December would have increased (decreased) equity and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant. The impact of income taxes is not reflected in this analysis:

	31 December 2013		**31 December 2012**	
'000 LVL	**Profit or loss, Bank**	**Profit or loss, Group**	**Profit or loss, Bank**	**Profit or loss, Group**
5% appreciation of USD against LVL	6	4	8	8
5% depreciation of USD against LVL	(6)	(4)	(8)	(8)
10% appreciation of RUB against LVL	11	11	1	1
10% depreciation of RUB against LVL	(11)	(11)	(1)	(1)

Price risk

Price risk is the risk that the value of a financial instrument will fluctuate as a result of changes in market prices, whether those changes are caused by factors specific to the individual instrument or factors affecting all instruments traded in the market. Price risk arises when the Group takes a long or short position in a financial instrument.

An analysis of sensitivity of the Group's net income for the year and equity to changes in securities prices based on positions existing as at 31 December 2013 and 2012 and a simplified scenario of a 5% change in all securities prices is as follows:

	31 December 2013		31 December 2012	
'000 LVL	**Profit or loss**	**OCI**	**Profit or loss**	**OCI**
5% increase in securities prices	6	351	-	-
5% decrease in securities prices	(6)	(351)	-	-

Results are the same for the Bank and for the Group because the subsidiary did not have investments in securities.

Credit risk

Credit risk is the risk of financial loss occurring as a result of default by a borrower or counterparty on their obligation to the Group. The Group has developed policies and procedures for the management of credit exposures (both for on balance sheet and off balance sheet exposures), including guidelines to limit portfolio concentration and the establishment of Limits Committee and Credit Committee, which actively monitor the Group's credit risk. The Group's credit policy is reviewed and approved by the Management Board and Council.

The Group's credit policy establishes:

- Procedures for review and approval of loan/credit applications;
- Methodology for the credit assessment of borrowers (corporate, SME and retail);
- Methodology for the credit assessment of counterparties, issuers and insurance companies;
- Methodology for the evaluation of collateral;
- Credit documentation requirements;
- Procedures for the ongoing monitoring of loans and other credit exposures.

Corporate loan/credit applications are originated by the relevant client managers or by Loan Department managers and are then passed on to the Loan Department. Loan Department's credit analysts prepare overall description report about credit deal, Financial Risk Management Department's analysts prepare risk report based on a structured analysis focusing on the customer's business and financial performance, as also a check that credit policy requirements have been met is made. Additional report is prepared by Security Department. The Credit Committee reviews the loan/credit application on the basis of submissions by the Loan Department, Financial Risk Management Department and Security Department. Individual transactions are also reviewed by the Group's Legal and Accounting departments depending on the specific risks and pending final approval of the Credit Committee.

The Group continuously monitors the performance of individual credit exposures and regularly reassesses the creditworthiness of its customers. The review is based on the customer's most recent financial statements and other information submitted by the borrower, or otherwise obtained by the Group. The current market value of collateral is regularly assessed by either independent appraisal companies or the Group's specialists, and in the event of negative movements in market prices the borrower is usually requested to put up additional security.

Apart from individual customer analysis, the whole credit portfolio is assessed by the Financial Risk Management Department with regard to credit concentration and market risks.

The Group's maximum exposure to on balance sheet credit risk is generally reflected in the carrying amounts of financial assets on the balance sheet. The impact of possible netting of assets and liabilities to reduce potential credit exposure at 31 December 2013 was LVL 954 thousand (2012: LVL 0 thousand).

The Group monitors concentrations of credit risk by industry/sector and by geographic location. For the analysis of concentration of credit risk in respect of loans and advances to customers refer to Note 21 "Loans and advances due from customers".

Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset. Liquidity risk exists when the maturities of assets and liabilities do not match. The matching and/or controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of financial institutions, including the Group. The Group maintains liquidity management with the objective of ensuring that funds will be available at all times to honour all cash flow obligations as they become due. The Group's liquidity policy is reviewed and approved by the Management Board and the Council.

The Group seeks to actively support a diversified and stable funding base from corporate and retail customer deposits, accompanied by diversified portfolios of highly liquid assets, in order to be able to respond quickly and smoothly to unforeseen liquidity requirements.

The liquidity management policy of the Group requires:

- projecting cash flows and considering the level of liquid assets necessary in relation thereto;
- maintaining a diversified deposits base;
- managing the concentration and profile of debts;
- maintaining debt financing plans;
- maintaining a portfolio of highly marketable assets that can easily be liquidated as protection against any interruption to cash flow;
- maintaining liquidity and funding contingency plans;
- monitoring balance sheet liquidity ratios against regulatory requirements, as also internal liquidity risk ratios and early warning indicators.

The Financial Market Department receives information from business units regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future business. The Financial Market Department then provides for an adequate portfolio of short-term liquid assets to be maintained, largely made up of short-term liquid trading securities, loans to banks and other inter-bank facilities, to ensure that sufficient liquidity is maintained within the Group as a whole.

The daily liquidity position is monitored and regular liquidity stress testing under a variety of scenarios covering both normal and more severe market conditions is performed by the Financial Risk Management Department. Under the normal market conditions, liquidity reports covering the liquidity position of the Group are presented to Limits Committee on a weekly basis. Decisions on the Group's liquidity management are made by the Limits Committee and implemented by the Financial Market Department.

The Group also calculates mandatory liquidity ratios on a daily basis in accordance with the requirement of the Financial and Capital Markets Commission. The Bank was in compliance with these ratios during the twelve-month period ended 31 December 2012 and 31 December 2013.

The table below analyses the Group's non-derivative financial liabilities and net-settled derivative financial liabilities into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. Derivative financial liabilities are included in the analysis if their contractual maturities are essential for an understanding of the timing of the cash flows. The amounts disclosed in the table are the contractual undiscounted cash flows.

Analysis of the Group's financial liabilities' contractual undiscounted cash flows as at 31 December 2013:

'000 LVL	Demand and less than 1 month	From 1 to 3 months	From 3 to 6 months	From 6 to 12 months	More than 1 year	Total gross amount outflow/ (inflow)	Carrying amount
Non-derivative liabilities							
Current accounts and deposits due to customers	7 418	971	2 130	3 031	1 187	14 737	14 534
Other borrowed funds	-	-	24	24	1 778	1 826	1 409
Derivative liabilities							
- Inflow	(101)	(417)	(126)	(186)	(668)	(1 498)	(1 489)
- Outflow	104	418	126	187	670	1 505	1 503
Total	**7 421**	**972**	**2 154**	**3 056**	**2 967**	**16 570**	**15 957**

The Group does not have any credit related commitments as at 31 December 2013.

Analysis of the Bank's financial liabilities' contractual undiscounted cash flows as at 31 December 2013:

'000 LVL	Demand and less than 1 month	From 1 to 3 months	From 3 to 6 months	From 6 to 12 months	More than 1 year	Total gross amount outflow/ (inflow)	Carrying amount
Non-derivative liabilities							
Current accounts and deposits due to customers	7 593	971	2 130	3 031	1 187	14 912	14 709
Other borrowed funds	-	-	24	24	1 778	1 826	1 409
Derivative liabilities							
- Inflow	(101)	(417)	(126)	(186)	(668)	(1 498)	(1 489)
- Outflow	104	418	126	187	670	1 505	1 503
Total	**7 596**	**972**	**2 154**	**3 056**	**2 967**	**16 745**	**16 132**

The Bank does not have any credit related commitments as at 31 December 2013.

Analysis of the Bank's financial liabilities' contractual undiscounted cash flows as at 31 December 2012:

'000 LVL	Demand and less than 1 month	From 1 to 3 months	From 3 to 6 months	From 6 to 12 months	More than 1 year	Total gross amount outflow/ (inflow)	Carrying amount
Non-derivative liabilities							
Current accounts and deposits due to customers	106	-	-	-	-	106	106
Total	**106**	**-**	**-**	**-**	**-**	**106**	**106**

The Bank did not have any credit related commitments as at 31 December 2012.

The Bank and the Group are keeping different financial assets to provide liquidity. Analysis of expected maturities of financial assets and liabilities and equity as at 31 December 2013 is presented below:

GROUP
'000 LVL

ASSETS	**1 month**	**1-3 months**	**3-6 months**	**6-12 months**	**Over 1 year**	**No maturity**	**Total**
Cash and due from central banks	1 788	-	-	-	-	-	**1 788**
Financial assets at fair value through profit or loss	104	6	-	-	-	-	**110**
Loans and advances due from financial institutions	7 843	285	212	766	-	-	**9 106**
Loans and advances due from customers	-	957	-	5	2 089	192	**3 243**
Available-for-sale financial assets	729	-	-	-	6 279	-	**7 008**
Held-to-maturity investments	155	265	-	104	675	-	**1 199**
Other financial assets	299	**-**	**-**	**-**	**-**	**-**	**299**
Total financial assets	**10 918**	**1 513**	**212**	**875**	**9 043**	**192**	**22 753**
LIABILITIES							
Financial assets at fair value through profit or loss	3	6	1	3	7	-	**20**
Current accounts and deposits due to customers	7 417	975	2 113	2 946	1083	-	**14 534**
Other borrowed funds	-	-	6	-	1 403	-	**1 409**
Total Liabilities	**7 420**	**981**	**2120**	**2 949**	**2 493**	**-**	**15 963**
Total Equity and reserves	-	-	-	-	-	9 034	**9 034**
Total Liabilities and Equity	**7 420**	**981**	**2 120**	**2 949**	**2 493**	**9 034**	**24 997**
Net liquidity position as at 31 December 2013	**3 498**	**532**	**(1 908)**	**(2 074)**	**6 550**	**(8 842)**	**-**
Net liquidity position as at 31 December 2012	1 638	10	21	(11)	85	(1 743)	-

BANK
'000 LVL

ASSETS	**1 month**	**1-3 months**	**3-6 months**	**6-12 months**	**Over 1 year**	**No maturity**	**Total**
Cash and due from central banks	1 788	-	-	-	-	-	**1 788**
Financial assets at fair value through profit or loss	104	6	-	-	-	-	**110**
Loans and advances due from financial institutions	7 661	106	-	766	-	-	**8 533**
Loans and advances due from customers	-	957	-	5	2 089	192	**3 243**
Available-for-sale financial assets	729	-	-	-	6 279	-	**7 008**
Held-to-maturity investments	155	265	-	104	675	-	**1 199**
Investment in subsidiary	-	-	-	-	-	1 317	**1 317**
Other financial assets	299	**-**	**-**	**-**	**-**	**-**	**299**
Total financial assets	**10 736**	**1 334**	**-**	**875**	**9 043**	**1 509**	**23 497**
LIABILITIES							
Financial assets at fair value through profit or loss	3	6	1	3	7	-	**20**
Current accounts and deposits due to customers	7 592	975	2 113	2 946	1 083	-	**14 709**
Other borrowed funds	-	-	6	-	1 403		**1 409**
Total Liabilities	**7 595**	**981**	**2 120**	**2 949**	**2 493**	**-**	**16 138**
Total Equity and reserves	**-**	**-**	**-**	**-**	**-**	**9 032**	**9 032**
Total Liabilities and Equity	**7 595**	**981**	**2 120**	**2 949**	**2 493**	**9 032**	**25 170**
Net liquidity position as at 31 December 2013	**3 141**	**353**	**(2 120)**	**(2 074)**	**6 550**	**(7 523)**	
Net liquidity position as at 31 December 2012	1 638	10	21	(11)	85	(1 743)	

Interest rate re-pricing analysis

The following table shows the Group's interest rate gap position as at 31 December 2013.

'000 LVL

ASSETS	**Less than 1 month**	**1 to 3 months**	**3 to 6 months**	**6 to 12 months**	**1 to 5 years**	**More than 5 years**	**Non-interest bearing financial instruments**	**Total**
Cash and due from central banks	597	-	-	-	-	-	1 191	**1 788**
Financial assets at fair value through profit or loss	-	-	-	-	-	-	110	**110**
Loans and advances due from financial institutions	118	285	212	766	-	-	7 725	**9 106**
Loans and advances due from customers	-	957	-	5	2 089	-	192	**3 243**
Available-for-sale financial assets	-	218	-	-	6 024	37	729	**7 008**
Held-to-maturity investments	155	265	-	104	675	-	-	**1 199**
Other financial assets	-	-	-	-	-	-	299	**299**
Long positions of interest rates risk sensitive off-balance items	101	417	126	186	668	-	-	**1 498**
Total assets and long off-balance-sheet positions sensitive to changes in interest rates	**971**	**2 142**	**338**	**1 061**	**9 456**	**37**	**10 246**	**24 251**
Financial assets at fair value through profit or loss	-	-	-	-	-	-	20	**20**
Current accounts and deposits due to customers	75	975	2 113	2 946	1 081	2	7 342	**14 534**
Other borrowed funds	-	-	6	-	-	1 403	-	**1 409**
Short positions of interest rates risk sensitive off-balance items	104	418	126	187	670	-	-	**1 505**
Total liabilities and short off-balance-sheet positions sensitive to changes in interest rates	**179**	**1 393**	**2 245**	**3 133**	**1 751**	**1 405**	**7 362**	**17 468**
Net position as at 31 December 2013	**792**	**749**	**(1 907)**	**(2 072)**	**7 705**	**(1 368)**	**2 884**	**6 783**
Net position as at 31 December 2012	1 552	1 552	1 552	1 552	1 552	1 552	**-**	9 312

The amounts in the tables above represent carrying amounts of the financial assets and liabilities as at the reporting date and do not include future interest payments.

The following table shows the Bank's interest rate gap position as at 31 December 2013.

'000 LVL

Financial assets	**Less than 1 month**	**1 to 3 months**	**3 to 6 months**	**6 to 12 months**	**1 to 5 years**	**More than 5 years**	**Non-interest bearing financial instruments**	**Total**
Cash and due from central banks	597	-	-	-	-	-	1 191	**1 788**
Financial assets at fair value through profit or loss	-	-	-	-	-	-	110	**110**
Loans and advances due from financial institutions	-	106	-	766	-	-	7 661	**8 533**
Loans and advances due from customers	13	954	-	5	2 079	-	192	**3 243**
Available-for-sale financial assets	-	218	-	-	6 024	37	729	**7 008**
Held-to-maturity investments	155	265	-	104	675	-	-	**1 199**
Investment in subsidiary	-	-	-	-	-	-	1 317	**1 317**
Other financial assets	-	-	-	-	-	-	299	**299**
Long positions of interest rates risk sensitive off-balance items	101	417	126	186	668	-	-	**1 498**
Total assets and long off-balance-sheet positions sensitive to changes in interest rates	**866**	**1 960**	**126**	**1 061**	**9 446**	**37**	**11 499**	**24 995**
Financial liabilities								
Financial assets at fair value through profit or loss	-	-	-	-	-	-	20	**20**
Current accounts and deposits due to customers	75	975	2 113	2 946	1 081	2	7 517	**14 709**
Other borrowed funds	-	-	6	-	-	1 403	-	**1 409**
Short positions of interest rates risk sensitive off-balance items	104	418	126	187	670	-	-	**1 505**
Total financial liabilities	**179**	**1 393**	**2 245**	**3 133**	**1 751**	**1 405**	**7 537**	**17 643**
Net position as at 31 December 2013	**687**	**567**	**(2 119)**	**(2 072)**	**7 695**	**(1 368)**	**3 962**	**7 352**
Net position as at 31 December 2012	1 552	1 552	1 552	1 552	1 552	1 552	**-**	9 312

The amounts in the tables above represent carrying amounts of the financial assets and liabilities as at the reporting date and do not include future interest payments.

Currency analysis

The following table shows Group's the currency structure of financial assets and liabilities at 31 December 2013:

'000 LVL **ASSETS**	**LVL**	**EUR**	**USD**	**other**	**Total**
Cash and due from central banks	652	1 014	63	59	**1 788**
Financial assets at fair value through profit or loss	-	-	110	-	**110**
Loans and advances due from financial institutions	4 365	1 542	3 169	30	**9 106**
Loans and advances due from customers	-	2 094	1 149	-	**3 243**
Available-for-sale financial assets	-	3 414	3 594	-	**7 008**
Held-to-maturity investments	-	675	369	155	**1 199**
Other assets	-	-	299	-	**299**
Total financial assets	**5 017**	**8 739**	**8 753**	**244**	**22 753**
Off-balance (SWAP)	**-**	**211**	**1 287**	**-**	**1 498**
LIABILITIES					
Financial assets at fair value through profit or loss	-	-	20	-	**20**
Current accounts and deposits due to customers	45	5 170	9 246	73	**14 534**
Other borrowed funds	-	1 058	351	-	**1 409**
Total Liabilities	**45**	**6 228**	**9 617**	**73**	**15 963**
Total Equity and reserves	9 034	-	-	-	9 034
Total Liabilities and Equity	**9 079**	**6 228**	**9 617**	**73**	**24 997**
Off-balance (SWAP)	**-**	**1 298**	**207**	**-**	**1 505**
Net currency balance position as at 31 December 2013	(4 062)	2 511	(864)	171	(2 244)
Net currency position as at 31 December 2013 (balance & off-balance)	**(4 062)**	**1 424**	**216**	**171**	**(2 251)**

The following table shows the Bank's the currency structure of financial assets and liabilities at 31 December 2013:

'000 LVL					
ASSETS	**LVL**	**EUR**	**USD**	**Other**	**Total**
Cash and due from central banks	652	1 014	63	59	**1 788**
Financial assets at fair value through profit or loss	-	-	110	-	**110**
Loans and advances due from financial institutions	4 363	1 016	3 127	27	**8 533**
Loans and advances due from customers	-	2 094	1 149	-	**3 243**
Available-for-sale financial assets	-	3 414	3 594	-	**7 008**
Held-to-maturity investments	-	675	369	155	**1 199**
Investment in subsidiary	1 317	-	-	-	**1 317**
Other financial assets	-	-	299	-	**299**
Total financial assets	**6 332**	**8 213**	**8 711**	**241**	**23 497**
Off-balance (SWAP)	**-**	**211**	**1 287**	**-**	**1 498**
LIABILITIES					
Financial assets at fair value through profit or loss	-	-	20	-	**20**
Current accounts and deposits due to customers	45	5 345	9 246	73	**14 709**
Other borrowed funds	-	1 058	351	-	**1 409**
Total Liabilities	**45**	**6 403**	**9 617**	**73**	**16 138**
Total Equity and reserves	9 032	-	-	-	**9 032**
Total Liabilities and Equity	**9 077**	**6 403**	**9 617**	**73**	**25 170**
Off-balance (SWAP)	**-**	**1 298**	**207**	**-**	**1 505**
Net currency balance position as at 31 December 2013	(2 745)	1 810	(906)	168	(1 673)
Total currency position as at 31 December 2013	(2 745)	723	174	168	(1 680)
Net currency position as at 31 December 2012	(172)	160	(4)	16	-
Total currency position as at 31 December 2012	76	65	118	-	259

Operational Risk

Operational risk is the risk of incurring losses resulting from inadequate or failed internal processes, which do not comply with the requirements of the external and internal legal regulations, the Bank's employees' and system activities, defects of internal processes, third parties' activities or from other external events as well, including legal risk, but excluding strategic and reputation risk. The aim of the management of the operational risk is to keep the operational risk on the economic reasonable minimum level, to stimulate stability of the Bank's activities and commercial profit in the long term.

The management of the operational risk goes through all the Bank's organizational structure and is realized in each unit of the Bank, that is why the management of the risk is based on overall comprehension of each employee of the Bank on processes he conducts and the risks inherent in these processes (high risk awareness), and on sound risk culture as well. The Bank does not accept operational risks, which exceed the Bank's risk appetite or if the impact of such risks cannot be evaluated in money terms and these risks at the same time are uncontrollable – it is impossible to prevent them or to insure against their consequences irrespective of economic benefit, which could arise from acceptance of such operational risks. In order to mitigate operational risk, the Bank uses the expert method and self-assessment; risk assessment prior launch of new products/process; implementation of quantitative indicators of operational risk; usage of database of risk events; stress – testing and scenario analysis.

Money Laundering and Terrorism Financing Risk

Money laundering and terrorism financing risk is the risk that the Bank can be involved into money laundering or terrorism financing. The Bank creates internal control system in the field of the ML/TF, observing requirements of the binding regulatory enactments and taking into account the best international practice, in order to prevent the use of financial services of the Bank for the ML/TF, dedicating the respective resources for that purpose and training employees. The Bank identifies each Client and applies due diligence procedures in accordance with a degree of the ML/TF risk of the Client. Depending on the degree of the ML/TF risk, the Bank investigates the nature of personal or economic activity of the Client, origin of funds in accounts held with the Bank and nature of transactions. The special client supervision structural units are established in the Bank that ensure due diligence of the Clients of the Bank prior to establishing business relations, supervision of transactions during business relations as well as exactly and timely performs duties of the Bank stipulated in the law in relations with competent state bodies. The Bank has the modest quantity of clients and it has deep knowledge of each of them which allows minimizing ML/TF risk.

Compliance and Reputation Risk

Compliance and reputation risk is the risk that the Bank is not subject to or in violation of the compliance legislation, losses may occur or may be imposed on the legal obligations or penalties may be applied or may degrade the reputation. The Bank has developed and implemented the "compliance policy" with the aim, of subject to compliance with the requirements in the legislation, to improve the Bank's capabilities and competitive position in the market; to strengthen confidence in the Bank; to protect the Bank's reputation, to lower the cost of capital; to reduce litigation and sanctions enforcement risks. To manage the compliance risk the Bank:

- Has established Compliance committee that has a central role in compliance risk management. Compliance committee evaluates and assesses identified compliance risks, decides on appropriate risks mitigation actions to be taken, monitors efficiency of compliance risks management.
- Keeps track of changes of compliance legislation and implements appropriate changes to internal normative documents of the Bank;
- Actively participates in the Committee of the Association of Latvian commercial banks, and FCMC held discussions/workshops on issues that affect the function of the competence of conformity;
- Evaluates the Bank internal normative documents and the lack of practical application;

- Analyzes and compares the performance data to ensure their compliance with certain requirements proactively;
- Analyzes the Bank customers' complaints.

Strategy Risk

Strategy risk is the risk that the changes in the business environment and the Bank's failure to respond to these changes timely, or false/unsubstantiated activities of the Bank's long-term strategy, or the Bank's inability to provide the necessary resources for the implementation of the strategy could adversely affect the Bank's income/expense (and the amount of equity capital). The Bank has developed operational development strategies, the implementation of which is regularly monitored and updated as necessary. The Bank plans its work with a variety of scenarios, including the negative scenarios that reflect the possible impact of adverse external conditions on the Bank's results.

Planning activities within the framework of development, the Bank carries out analysis of the external environment, competitiveness of the Bank, its position in the financial market, Bank's internal business environment, including macroeconomic circumstances, with the purpose to determine the likelihood that an event in a business environment, in which the Bank carries out its activities and/or intends to take action in the future, will have a negative impact on the Bank's ability to achieve its strategic objectives (to implement the strategy) and/or threaten the Bank's future operations. Evaluating and planning the Bank's asset and liability structure is based on results of analysis of selected indicators of development activities and the business environment.

5 Capital management

The Financial and Capital Market Commission sets and monitors capital requirements for the Bank and the Group.

The Bank and the Group defines as capital those items defined by statutory regulation as capital. Under the current capital requirements set by the Financial and Capital Market Commission, banks must maintain a ratio of capital to risk weighted assets ("statutory capital ratio") above the prescribed minimum level. As at 31 December 2013, the individual minimum level is set at 20%. The Bank was in compliance with the FCMC determined individual capital ratio during the year ended 31 December 2013 and 2012.

The Group's risk based capital adequacy ratio as at 31 December 2013 was 50.40% .

The Bank's risk based capital adequacy ratio as at 31 December 2013 was 57.44% (31 December 2012: 56.98%).

The Group monitors its capital adequacy levels calculated in accordance with the requirements of the Basle Accord, as defined in the International Convergence of Capital Measurement and Capital Standards (updated April 1998) and Amendment to the Capital Accord to incorporate market risks (updated November 2008), commonly known as Basel II, as adopted by FCMC regulations.

The following table shows the composition of the Group's capital position as at 31 December 2013:

'000 LVL	2013 Group	2013 Bank	2012 Bank
Tier 1 capital			
Share capital	19 622	19 622	12 235
Additional paid-in capital	20	20	20
Reserves	219	219	219
Retained earnings	(10 840)	(10 842)	(8 797)
Reductions of tier 1 capital	(917)	(363)	(2)
Total tier 1 capital	**8 104**	**8 656**	**3 675**
Tier 2 capital			
Subordinated debt (unamortised portion)	1 403	1 403	-
Total tier 2 capital	**1 403**	**1 403**	**-**
Deductions from Tier 1 and Tier 2 capital prescribed by legislation	-	-	-
Total capital	**9 507**	**10 059**	**3 675**
Capital requirements			
Credit risk requirements	1 212	1 273	224
Market risk requirements	168	108	14
Operational risk requirements	20	20	278
Capital requirement, which is equal to 25% of the previous year's fixed costs	109	-	-
Total capital requirements	**1 509**	**1 401**	**516**
Capital adequacy ratio	**50.40 %**	**57.44 %**	**56.98 %**
Tier 1 Capital adequacy ratio	**42.96 %**	**49.43 %**	**56.98 %**

The risk-weighted assets are measured by means of a hierarchy of risk weights classified according to the nature of assets and reflecting an estimate of credit, market and other risks associated with each asset and counterparty, taking into account any eligible collateral or guarantees. A similar treatment is adopted for off-balance sheet exposure, with some adjustments to reflect the more contingent nature of the potential losses.

The Group is subject to minimum capital adequacy requirements calculated in accordance with the Basel Accord established by covenants under liabilities incurred by the Group. The Group has complied with all externally imposed capital requirements during the years ended 31 December 2013 and 31 December 2012.

6 Use of estimates and judgements

The preparation of financial statements in conformity with IFRSs requires management to make judgments, estimates and assumptions that affect the application of policies and the reported amounts of assets and liabilities, income and expenses. Although these estimates are based on management's best knowledge of current events and actions, actual results ultimately may differ from those estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised prospectively.

These disclosures supplement the commentary on financial risk management (see note 4).

Key sources of estimation uncertainty:

Allowances for credit losses

Financial assets accounted for at amortised cost are evaluated for impairment on a basis described in accounting policy, note 3.

The specific counterparty component of the total allowances for impairment applies to financial assets evaluated individually for impairment and is based upon the Bank's management best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgements about a counterparty's financial situation and the net realisable value of any underlying collateral. Each impaired asset is assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable are independently approved by the Credit Risk function.

The Bank does not assess collective impairment allowance since the number of loans in the loan portfolio is too small and collective impairment assessment would not be practicable.

Impairment of financial instruments

The determination of impairment indication is based on comparison of the financial instrument's carrying value and fair value. The Group uses valuation models based on quoted market prices of similar products.

For the purposes of impairment loss measurement, the Bank's management makes estimates of any expected changes in future cash flows from a specific financial instrument based on analysis of financial position of the issuer of the financial instrument.

Measurement of fair values

A number of the Group's accounting policies and disclosures require the measurement of fair values, for both financial and non-financial assets and liabilities.

The Group has an established control framework with respect to the measurement of fair values.

Where third-party information, such as broker quotes or pricing services, are used to measure fair value, the Bank assesses and documents the evidence obtained from the third parties to support the conclusion that such valuations meet the requirements of IFRS. This includes:

- Verifying the that broker or pricing service is approved by the Group for use in pricing the relevant type of financial instrument;
- Understanding how the fair value has been arrived at and the extent to which it represents actual market transactions;
- When prices for similar instruments are used to measure fair value, how these prices have been adjusted to reflect the characteristics of the instrument subject to measurement;

When measuring the fair value of an asset or a liability, the Group uses market observable data as far as possible. Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the valuation techniques as follows:

Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

If the inputs used to measure the fair value of an asset or a liability might be categorised in different levels of the fair value hierarchy, the fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.

The Group recognises transfers between levels of the fair value hierarchy at the end of the reporting period during which the change has occurred.

Further information about the assumptions and judgments made in measuring fair values is included in Note 37 – Fair value of financial instruments.

7 Net interest income

'000 LVL	2013 Group	2013 Bank	2012 Bank
Interest income			
Interest income arising from financial assets not at fair value through profit or loss			
Loans and advances due from financial institutions	22	21	4
Loans and advances due from customers	25	25	-
Available-for-sale financial assets	55	55	-
Held-to-maturity investments	11	11	-
Total	**113**	**112**	**4**
Interest expense recognised on liabilities measured at amortised cost			
Current accounts and deposits due to customers	(31)	(31)	(2)
Other borrowed funds	(8)	(8)	(3)
Total	**(39)**	**(39)**	**(5)**

8 Fee and commission income

'000 LVL	2013 Group	2013 Bank	2012 Bank
Settlement fees	26	26	37
Brokerage fees	3	3	-
Trust, custodian and other fiduciary services fees	86	50	-
Other	7	6	1
Total	**122**	**85**	**38**

9 Fee and commission expense

'000 LVL	2013 Group	2013 Bank	2012 Bank
Custodian fees	38	37	-
Settlement fees	22	21	13
Total	**60**	**58**	**13**

10 Net gain/(loss) on financial assets at fair value through profit or loss

'000 LVL	2013 Group	2013 Bank	2012 Bank
Investment funds	(14)	(14)	-
Total	**(14)**	**(14)**	**-**

11 Net foreign exchange income/(loss)

'000 LVL	2013 Group	2013 Bank	2012 Bank
Gain/(loss) from revaluation of financial assets and liabilities	25	25	(4)
Total	**25**	**25**	**(4)**

12 Net realized gain/(loss) on Available-for-sale financial assets

'000 LVL	2013 Group	2013 Bank	2012 Bank
Debt instruments	16	16	-
Total	**16**	**16**	**-**

13 Other income

'000 LVL	2013 Group	2013 Bank	2012 Bank
Rental income	1	2	-
Other income	28	27	109
Total	**29**	**29**	**109**

14 General administrative expenses

'000 LVL	2013 Group	2013 Bank	2012 Bank
Employee compensation	1 088	1 067	758
Payroll related taxes	267	262	180
Depreciation and amortization	181	176	123
Repairs and maintenance	105	105	168
Communications and information services	103	103	75
Rent	101	101	83
Professional services	101	101	218
Payment cards expenses	99	99	-
IT service costs	64	62	-
Other	58	57	173
Travel expenses	20	20	6
Advertising and marketing	13	13	6
Security	7	7	140
Total	**2 207**	**2 173**	**1 930**

15 Other expenses

'000 LVL	2013 Group	2013 Bank	2012 Bank
Provisions for contingent liability	-	-	96
Total	**-**	**-**	**96**

16 Impairment loss

'000 LVL	2013 Group	2013 Bank	2012 Bank
Impairment losses			
Other non-financial assets	49	49	-
Net impairment losses	**49**	**49**	**-**

Analysis of changes in impairment allowances of the Group and the Bank:

'000 LVL	Allowance for other assets
Allowances as of 31 Dec 2012	-
Impairment charge	49
Allowances as of 31 Dec 2013	**49**

The Bank has created an impairment allowance for the claim against one of it service provider.

17 Income tax benefit

(a) Income tax recognised in the profit or loss

'000 LVL

	2013 Group	**2013 Bank**	**2012 Bank**
Deferred tax benefit			
Utilization of unrecognized tax losses carried forward	21	21	-
Origination and reversal of temporary differences	-	-	2
Total income tax benefit recognised in profit or loss	**21**	**21**	**2**

(b) Reconciliation of effective tax rate:

'000 LVL	**2013 Group**	**2013 Bank**	**2012 Bank**
Loss before income tax	**(2 064)**	**(2 066)**	**(1 897)**
Theoretically calculated tax at tax rate of 15%	(310)	(310)	(285)
Non-deductible costs/(non-taxable income)	(21)	(21)	(2)
Change in unrecognised deferred tax assets	310	310	285
Income tax benefit	**(21)**	**(21)**	**(2)**

18 Cash and cash equivalents

Cash and cash equivalents at the end of the financial year as shown in the statement of cash flow are composed of the following items:

'000 LVL	31 Dec 2013 Group	31 Dec 2013 Bank	31 Dec 2012 Bank
Cash	214	214	107
Balances due from central banks	1 574	1 574	287
Subtotal	**1 788**	**1 788**	**394**
Demand deposit due from financial institutions	7 726	7 662	1 371
Total	**9 514**	**9 450**	**1 765**

19 Financial assets at fair value through profit or loss

	31 Dec 2013 Group	31 Dec 2013 Bank	31 Dec 2012 Bank
Non-fixed income investments			
Investments funds	104	104	-
Derivative financial instruments			
Foreign currency contracts	6	6	-
	110	**110**	**-**
Liabilities			
Derivative financial instruments			
Foreign currency contracts	20	20	-
	20	**20**	**-**
Net financial assets at fair value **through profit or loss**	**90**	**90**	**-**

Included in financial assets at fair value through profit or loss at 31 December 2013 are LVL 104 thousand (2012: LVL 0 thousand) in financial instruments which are classified as held for trading and LVL 14 thousand (2012: LVL 0 thousand) net liabilities in financial instruments which were, upon initial recognition, designated by the entity as financial assets at fair value through profit or loss.

20 Loans and advances due from financial institutions

'000 LVL	31 Dec 2013 Group	31 Dec 2013 Bank	31 Dec 2012 Bank
Not impaired or past due			
Nostro accounts			
Latvian commercial banks	6 586	6 522	27
OECD banks	922	922	41
Non-OECD banks	218	218	3
Assigned ratings[2]			
Rated A- and above	922	922	41
Rated from BBB- to BBB+	18	18	26
Rated from BB- to BB+	98	98	3
Not rated	6 688	6 624	1
Assigned and parents ratings[3]			
Rated A- and above	7 508	7 444	42
Rated from BBB- to BBB+	18	18	26
Rated from BB- to BB+	98	98	3
Not rated	102	102	
Total nostro accounts	**7 726**	**7 662**	**71**
Loans and deposits			
Latvian commercial banks	614	105	1 300
Non-OECD banks	766	766	-
Assigned ratings[2]			
Rated from BB- to BB+	766	766	-
Rated B+ and below	118	-	400
Not rated	496	105	900
Assigned and parents ratings[3]			
Rated A- and above	496	105	900
Rated from BBB- to BBB+			
Rated from BB- to BB+	766	766	-
Rated B+ and below	118	-	400
Not rated	-	-	-
Total loans and deposits not impaired	**1 380**	**871**	**1 300**
Total	**9 106**	**8 533**	**1 371**

[2] Loans and advances due from financial institutions are classified by average credit rating from three international rating agencies: Moody's Investors Service, Standard & Poor's, Fitch Ratings.

[3] Classification is based on credit ratings of parental banks for these Latvian commercial banks: "Swedbank" AS, AS "SEB Banka", AS "DNB banka".

No impairment was made for loans and advances due from financial institutions.

Concentration of placements with banks and other financial institutions

As at 31 December 2013 and 2012 the Group and the Bank had two banks and financial institutions, whose balances exceeded 10% of total placements with banks and other financial institutions. The gross value of these balances as of 31 December 2013 and 2012 were LVL 6 522 thousand and LVL 1 300 thousand, respectively.

21 Loans and advances due from customers

'000 LVL	31 Dec 2013 Group	31 Dec 2013 Bank	31 Dec 2012 Bank
Loans to customers			
Business loans	3 046	3 046	-
Other	197	197	198
Total loans to customers	**3 243**	**3 243**	**198**

Since the loans to customers have been issued close to the end of the reporting period and no impairment indications have been identified as at 31 December 2013, the Bank has not made impairment allowances for loans to customers.

Geographical analysis of the loan portfolio

'000 LVL	31 Dec 2013 Group	31 Dec 2013 Bank	31 Dec 2012 Bank
Latvia	5	5	-
OECD countries	192	192	198
Non-OECD countries	3 046	3 046	-
	3 243	**3 243**	**198**
Impairment allowance	-	-	-
	3 243	**3 243**	**198**

Significant credit exposures

As at 31 December 2013 the Group and the Bank had two borrowers, whose loan balances exceeded 10% of loans to customers. The gross value of these loans as of 31 December 2013 was LVL 3 046 thousand (2012: LVL 198 thousand).

According to regulatory requirements, the Group is not allowed to have a credit exposure to one client or group of related clients more than 25% of its equity. As at 31 December 2013 and 31 December 2012 the Group was in compliance with this requirement.

22 Available-for-sale financial assets

'000 LVL	31 Dec 2013 Group	31 Dec 2013 Bank	31 Dec 2012 Bank
Debt and other fixed-income instruments			
- Government and municipal bonds			
Latvia	424	424	-
European Union	829	829	-
Total government and municipal bonds	**1 253**	**1 253**	**-**
- Corporate bonds			
Latvia	809	809	-
European Union and EEA	2 517	2 517	-
Russia	1 540	1 540	-
Other countries	160	160	-
Total corporate bonds	**5 026**	**5 026**	-
Total debt and other fixed-income instruments	**6 279**	**6 279**	**-**
Government and municipal bonds[4]			
Rated from BBB- to BBB+	1 253	1 253	-
Total government and municipal bonds	**1 253**	**1 253**	**-**
Corporate bonds			
Rated A- and above	793	793	-
Rated from BBB- to BBB+	1 233	1 233	-
Rated from BB- to BB+	1 133	1 133	-
Rated B+ and below	631	631	-
Not rated	1 236	1 236	-
Total corporate bonds	**5 026**	**5 026**	**-**
Total debt and other fixed-income instruments	**6 279**	**6 279**	
Non-fixed income investments			
Investment funds	729	729	-
Total non-fixed income investments	**729**	**729**	**-**
Total Available-for-sale financial assets	**7 008**	**7 008**	**-**

[4] Available-for-sale financial assets are classified by average credit rating from three international rating agencies: Moody's Investors Service, Standard & Poor's, Fitch Ratings.

23 Held-to-maturity investments

'000 LVL	31 Dec 2013 Group	31 Dec 2013 Bank	31 Dec 2012 Bank
Debt and other fixed-income instruments			
- Government and municipal bonds			
European Union and EEA	675	675	-
Total government and municipal bonds	**675**	**675**	**-**
- Promissory notes			
Russia	524	524	-
Total promissory notes	**524**	**524**	**-**
Total debt and other fixed-income instruments	**1 199**	**1 199**	**-**

Debt and other fixed-income instruments			
- Government and municipal bonds[5]			
Rated from BB- to BB+	675	675	-
Total government and municipal bonds	**675**	**675**	**-**
- Promissory notes			
Not rated	524	524	-
Total promissory notes	**524**	**524**	**-**
Total debt and other fixed-income instruments	**1 199**	**1 199**	**-**

Geographical allocation is based on risk of countries of issuers.

[5] Held-to-maturity investments are classified by average credit rating from three international rating agencies: Moody's Investors Service, Standard & Poor's, Fitch Ratings.

24 Investment in subsidiary

'000 LVL	31 Dec 2013	31 Dec 2012
Investments in „M2M Asset Management" IPAS	1 317	-
Impairment allowance	-	-
	1 317	**-**

	„M2M Asset Management" IPAS
Main activity	Financial services
Country of incorporation	Latvia
Ownership interest	
31 December 2012	-
31 December 2013	100 %

'000 LVL	
As at 31 Dec 2013	
Non-current assets	12
Current assets	770
Non-current liabilities	-
Current liabilities	(17)
Net assets	**765**
Group share in net assets as at 31 Dec 2013	**100 %**
For year 2013	
Income	217
Expenses	(368)
Profit or loss	**(151)**
Group share in profit for 2013	**1 %**
Carrying amount	
31 December 2013	**1 317**

During the year ended 31 December 2013 the Group did not receive dividends from investment in subsidiary.

Further information about the acquisition of the subsidiary is disclosed in Note 39 – Acquisitions and disposals.

25 Property and equipment

Group '000 LVL	Leasehold improvements	Other	Total
Cost			
At 1 January 2013	918	1 161	2 079
Additions	-	52	52
Acquisitions through business combinations	-	24	24
Disposals	-	(37)	(37)
Transfers to Leasehold improvements and Intangible assets	412	(728)	(316)
At 31 December 2013	**1 330**	**472**	**1 802**
Depreciation			
At 1 January 2013	170	175	345
Acquisitions through business combinations	-	7	7
Depreciation charge	72	97	169
Disposals	-	(37)	(37)
At 31 December 2013	**242**	**242**	**484**
Carrying value			
At 31 December 2013	**1 088**	**230**	**1 318**

25 Property and equipment, continued

Bank **'000 LVL**	**Leasehold improvements**	**Other**	**Total**
Cost			
At 1 January 2013	918	1 161	2 079
Additions	-	52	52
Disposals	-	(37)	(37)
Transfers to Leasehold improvements and Intangible assets	412	(728)	(316)
At 31 December 2013	**1 330**	**448**	**1 778**
Depreciation			
At 1 January 2013	170	175	345
Depreciation charge	72	92	164
Disposals	-	(37)	(37)
At 31 December 2013	**242**	**230**	**472**
Carrying value			
At 31 December 2013	**1 088**	**218**	**1 306**
At 31 December 2012	748	986	1 734

25 Property and equipment, continued

Bank **'000 LVL**	**Leasehold improvements**	**Other**	**Total**
Cost			
At 1 January 2012	918	1 132	2 050
Additions	-	55	55
Disposals	-	(7)	(7)
Transfers	-	(19)	(19)
At 31 December 2012	**918**	**1 161**	**2 079**
Depreciation			
At 1 January 2012	150	80	230
Depreciation charge	20	102	122
Disposals	-	(7)	(7)
At 31 December 2012	**170**	**175**	**345**
Carrying value			
At 31 December 2012	**748**	**986**	**1 734**
At 31 December 2011	768	1 052	1 820

26 Goodwill and other intangible assets

Group

'000 LVL	**Goodwill**	**Software**	**Other**	**Total**
Cost				
At 1 January 2013	-	-	3	3
Additions[6]	554	-	57	611
Transfers from other assets	-	316	-	316
At 31 December 2013	**554**	**316**	**60**	**930**
Amortization				
At 1 January 2013	-	-	1	1
Amortization charge	-	11	1	12
At 31 December 2013	**-**	**11**	**2**	**13**
Carrying value				
At 31 December 2013	**554**	**305**	**58**	**917**
At 31 December 2012	-	-	2	2

[6] See Note 39 for additional information on goodwill.

26 Goodwill and other intangible assets, continued

Bank

'000 LVL	**Software**	**Other**	**Total**
Cost			
At 1 January 2013	-	3	3
Additions	-	57	57
Transfers from other assets	316	-	316
At 31 December 2013	**316**	**60**	**376**
Amortization			
At 1 January 2013	-	1	1
Amortization charge	11	1	12
At 31 December 2013	**11**	**2**	**13**
Carrying value			
At 31 December 2013	**305**	**58**	**363**
At 31 December 2012	-	2	2
Cost			
At 1 January 2012	-	3	3
Additions	-	3	3
Transfers	-	(3)	(3)
At 31 December 2012	**-**	**3**	**3**
Amortization			
At 1 January 2012	-	2	2
Amortization charge	-	1	1
Transfers	-	(2)	(2)
At 31 December 2012	**-**	**1**	**1**
Carrying value			
At 31 December 2012	**-**	**2**	**2**
At 31 December 2011	-	1	1

27 Other assets

'000 LVL	31 Dec 2013 Group	31 Dec 2013 Bank	31 Dec 2012 Bank
Other financial assets			
Receivables from brokers	299	299	-
Other financial assets	**299**	**299**	**-**
Other non-financial assets			
Prepayments	196	196	42
Accrued income	12	12	284
VAT overpaid	16	16	-
Other	110	88	211
Impairment allowance	(49)	(49)	-
Other non-financial assets	**285**	**263**	**537**
	584	**562**	**537**

28 Current accounts and deposits due to customers

'000 LVL	31 Dec 2013 Group	31 Dec 2013 Bank	31 Dec 2012 Bank
Current accounts and demand deposits	**7 364**	**7 539**	**106**
- Private individual	2 470	2 470	105
- Corporate	4 894	5 069	1
Term deposits	**7 170**	**7 170**	**-**
- Private individual	3 380	3 380	-
- Corporate	3 790	3 790	-
	14 534	**14 709**	**106**

Concentrations of current accounts and customer deposits

As of 31 December 2013, the Group had two customers, whose balances exceeded 10% of total customer accounts. These balances as of 31 December 2013 were LVL 4 579 thousand (2012: LVL 81 thousand).

29 Subordinated debt

'000 LVL	31 Dec 2013 Group	31 Dec 2013 Bank	31 Dec 2012 Bank
Subordinated borrowings	1 409	1 409	-
	1 409	**1 409**	**-**

Subordinated borrowings have a fixed term of at least five years at their origination, and are repayable before maturity only on winding up of the issuer. In the event of the winding-up of the issuer these borrowings will be subordinated to the claims of depositors and all other creditors of the issuer.

30 Deferred tax asset and liability

Temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes give rise to net deferred tax assets and liabilities as of 31 December 2013 and 2012. These deferred tax assets have not been recognised in these consolidated financial statements.

Movement in temporary differences during the year ended 31 December 2013 of the Group and the Bank:

				31 December 2013	
'000 LVL	Net balance 1 January 2013	Recognised in profit or loss	Net balance 31 December 2013	Deferred tax asset	Deferred tax liability
Deferred Holiday Pay	2	5	7	7	-
Property and equipment	(23)	2	(21)	-	(21)
Impairment of non-financial assets	-	7	7	7	-
Tax loss carry-forwards	-	7	7	7	-
Deferred tax assets (liabilities) before set-off	**(21)**	**21**	**-**	**21**	**(21)**
Set off of tax				(21)	21
Net deferred tax assets				**-**	**-**

Unrecognised deferred tax asset

Deferred tax asset of the Bank on tax losses carried forward of LVL 1 626 thousand (2012: LVL 1 320 thousand) have not been recognised, because it is not probable that future taxable profit will be available against which the Bank can use the benefits there from.

Deferred tax asset of the subsidiary on tax losses carried forward of LVL 95 thousand (2012: LVL 72 thousand) have not been recognised, because it is not probable that future taxable profit will be available against which the Group and the Bank can use the benefits there from.

31 Provisions and contingent liabilities

In the ordinary course of business, the Group and is subject to legal actions and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints, will not have a material adverse effect on the financial conditions of the results of the future operations of the Group.

Timing of the contingent liability is uncertain and the Group is not exposed to adverse profit or loss statement effects since it has created provisions in full amount for the potential claim.

32 Other liabilities

'000 LVL	**31 Dec 2013 Group**	**31 Dec 2013 Bank**	**31 Dec 2012 Bank**
Accrued expenses	51	50	-
Payables on securities settlements	19	19	-
Provision for employee vacations	85	73	29
Other	32	28	311
	187	**170**	**340**

33 Share capital and treasury shares

Issued capital and share premium

In 2013 the share capital of Bank M2M Europe AS was increased three times – in February, May and September by a total of LVL 7 386 800.

During the reporting period previous shareholders have sold 100% of shares to the new owner Andrey Vdovin

The share capital of the Bank amounts to LVL 19 622 400 (2012: LVL 12 235 600) and consists of 392 488 (2012: 244 712) name shares with voting rights. Nominal value of each share is LVL 50 (2012: LVL 50). All shares of the Bank are dematerialized name shares.

Reserves

Other reserves represent residual interest of shareholders and can be distributed to them.

34 Operating leases

Operating lease rentals are payable as follows:

'000 LVL	**31 Dec 2013 Group**	**31 Dec 2013 Bank**	**31 Dec 2012 Bank**
Less than one year	97	98	106
Between one and five years	390	390	415
More than five years	911	911	3 154
	1 398	**1 399**	**3 675**

The Bank leases its headquarters under operating lease. The lease runs for an initial period of fifteen years, with an option to renew the lease after that date. Lease payments are fixed. None of the leases includes contingent rentals.

During the current year LVL 101 thousand was recognised as an expense in the statement of loss in respect of operating leases (2012: LVL 83 thousand).

35 Assets management

Assets management services

The Group through its Subsidiary provides assets management services to individuals and institutions. The Group receives management fee for providing these services. The assets under management of the Subsidiary are not included in neither the consolidated and nor separate statement of financial position. As of 31 December 2013 the Group had LVL 43 530 thousand (2012: LVL 39 093 thousand)[7] assets under management of which the Bank held LVL 2 360 (2012: LVL 0 thousand) thousand.

Custody activities

The Group and the Bank provides custody services to its customers, whereby it holds securities on behalf of customers and receives fee income for providing these services. These securities are neither assets of the Group, nor the Bank and are not recognised in the consolidated and separate statements of financial position. As of 31 December 2013 the total amount in custody on behalf of customers was LVL 16 636 thousand.

36 Related party transactions

Transactions with members of the Board of Directors and the Management Board of the Group and the Bank

Total remuneration included in employee compensation (refer Note 14):

'000 LVL	**2013 Group**	**2013 Bank**	**2012 Bank**
Members of the Management Board	267	249	206
	267	**249**	**206**

[7] Assets under management of M2M Asset Management IPAS at the end of 2012 prior acquisition by the Bank.

The outstanding balances and average interest rates as of 31 December 2013 with members of the Council and the Management Board are as follows:

	2013 '000 LVL	**2012 '000 LVL**
Statement of financial position		
Liabilities		
Current accounts	21	-

Transactions with related parties of the Bank

The outstanding balances as of 31 December 2013 and related profit or loss amounts of transactions for the year ended 31 December 2013 with other related parties are as follows.

'000 LVL	**Subsidiary company**	**Other**	**Total**
Statement of financial position			
Assets			
Loans and advances due from financial institutions	-	102	102
Financial assets at fair value through profit or loss	-	523	523
Total assets	-	625	625
Liabilities			
Deposits and balances due to financial institutions	175	408	583
Payables for management services	-	11	11
Total liabilities	175	419	594
Income/(expenses)			
Fee and commission income	1	6	7
Administrative expenses	-	(11)	(11)

The subsidiary has no other related party transactions than those with the Bank. Therefore, transactions with related parties of the Group are not disclosed separately.

37 Fair value of financial instruments

Financial instruments measured at fair value

The table below analyses financial instruments measured at fair value the Group and the Bank at the end of the reporting period, by the level in the fair value hierarchy into which the fair value measurement is categorised.

	Level 1	**Level 2**	**Level 3**	**Total**
2013	**'000 LVL**	**'000 LVL**	**'000 LVL**	**'000 LVL**
Financial assets				
Financial assets at fair value through profit or loss	104	6	-	110
Available for sale instruments	6 199	809	-	7 008
	6 303	**815**	**-**	**7 118**
Financial liabilities				
Financial assets at fair value through profit or loss	-	20	-	20
	-	**20**	**-**	**20**
2012				
Financial assets				
	-	**-**	**-**	**-**
Financial liabilities				
	-	**-**	**-**	**-**

37 Fair value of financial instruments, continued

Financial instruments not measured at fair value

The table below analyses the fair values of financial instruments not measured at fair value of the Group, by the level in the fair value hierarchy into which each fair value measurement is categorised:

31 December 2013	Level 1 '000 LVL	Level 2 '000 LVL	Level 3 '000 LVL	Total fair values '000 LVL	Total carrying amount '000 LVL
Financial assets					
Cash and due from central banks[1)]	-	-	-	1 788	1 788
Loans and advances due from financial institutions[2)]	-	-	-	9 106	9 106
Loans and advances due from customers[3)]	-	-	-	3 243	3 243
Held to maturity instruments	684	481	-	1 165	1 199
Other financial assets[4)]	-	-	-	299	299
Financial liabilities					
Deposits and balances due to customers	-	-	14 541	14 541	14 534
Other borrowed funds	-	-	1 373	1 373	1 409

1) Cash and due from central banks are various currency cash and deposits with the Bank of Latvia whose carrying amount represents the fair value.
2) Most of the loans and advances due from financial institutions are either deposits on demand or short term deposits; therefore, their carrying amount approximates the fair value.
3) Since the loans were issued close to the reporting date, their carrying amount of loans and advances due from financial institutions approximates the fair value.
4) Other financial assets consist of receivables from settlement of financial instruments; thus the carrying amount is equal to their fair value.

37 Fair value of financial instruments, continued

The table below analyses the fair values of financial instruments not measured at fair value of the Bank, by the level in the fair value hierarchy into which each fair value measurement is categorised:

31 December 2013	Level 1	Level 2	Level 3	Total fair values	Total carrying amount
	'000 LVL	'000 LVL	'000 LVL	'000 LVL	'000 LVL
Financial assets					
Cash and due from central banks[1)]	-	-	-	1 778	1 788
Loans and advances due from financial institutions[2)]	-	-	-	8 533	8 533
Loans and advances due from customers[3)]	-	-	-	3 243	3 243
Held to maturity instruments	684	481	-	1 165	1 199
Other financial assets[4)]	-	-	-	299	299
Financial liabilities					
Deposits and balances due to customers	-	-	14 716	14 716	14 709
Other borrowed funds	-	-	1 373	1 373	1 409

1) Cash and due from central banks consist of various currency cash and deposits with the Bank of Latvia whose carrying amount represents the fair value.
2) Most of the loans and advances due from financial institutions are either deposits on demand or short term deposits; therefore, their carrying amount approximates the fair value.
3) Since the loans were issued close to the reporting date, their carrying amount of loans and advances due from financial institutions approximates the fair value.
4) Other financial assets consist of receivables from settlement of financial instruments; thus the carrying amount is equal to their fair value.

37 Fair value of financial instruments, continued

'000 LVL **31 December 2012**	**Total fair values**	**Total carrying amount**
Financial assets		
Cash and due from central banks	394	394
Loans and advances due from financial institutions	1 371	1 371
Loans and advances due from customers	198	198
Other financial assets	-	-
Financial liabilities		
Deposits and balances due to customers	106	106
Other borrowed funds	-	-
Other financial liabilities	-	-

The following table shows the valuation techniques use in measuring Level 2 and Level 3 fair values, as well as the significant unobservable inputs used:

Financial instruments measured at fair value

Type	**Valuation technique**	**Significant unobservable inputs**
Financial assets at fair value through profit or loss	Discounted cash flows	Discount rates
Available for sale instruments	Discounted cash flows	Discount rates

37 Fair value of financial instruments, continued

Financial instruments not measured at fair value

Type	Valuation technique	Significant unobservable inputs
Loans and advances due from financial institutions	Discounted cash flows	Discount rates
Loans and advances due from customers	Discounted cash flows	Discount rates
Deposits and balances due to customers	Discounted cash flows	Discount rates
Other borrowed funds	Discounted cash flows	Discount rates

38 Events subsequent to the reporting date

On 1 January 2014 the Republic of Latvia joined the eurozone and the Latvian lat was replaced by the euro. As a result, AS Bank M2M Europe translated its financial accounting to euros as from 1 January 2014 and the financial statements for subsequent years will be prepared and presented in euros. Future comparative information will be translated into euros using the official exchange rate of LVL 0.702804 to EUR 1.

39 Acquisitions and disposals

Acquisition of subsidiary

On November 11, 2013 the Bank acquired all of the shares in M2M Asset Management IPAS for LVL 1 316 800, which was settled in cash. The subsidiary was acquired from the shareholder of the Bank and the deal was assessed to have taken place on market transaction terms.

If the acquisition had occurred on 1 January 2013 Group interest income for the year would have been LVL 329 thousand and the loss for the year would have been LVL 2 196 thousand. In determining these figures it has been assumed that like described below in relation to the acquisition date there would have been no fair value adjustments at 1 January 2013.

As of 31.12.2013 the Group did not identify any fair value adjustments to the carrying amounts of the assets and liabilities of the acquired subsidiary as of the acquisition date.

39 Acquisitions and disposals, continued

The acquisition of the subsidiary had the following effect on the Group's assets and liabilities at the date of acquisition:

'000 LVL	**Recognised fair value on acquisition**
Assets	**777**
Loans and advances due from financial institutions	744
Property and equipment	17
Other assets	16
Liabilities	**(14)**
Other liabilities	(14)
Net identifiable assets and liabilities	**763**
Goodwill on acquisition	554
Consideration paid	1 317
Cash acquired	(743)
Net cash outflow	**574**

Goodwill arising on the acquisition is attributable to M2M Asset Management IPAS developed product range, skills of work force and the synergies expected to be achieved from integrating the company into the Bank's existing business. None of the goodwill recognised is expected to be deductible for tax purposes.