

*The Statement is published taking into account the provisions of the Financial and Capital Market Commission "Regulations on the Information Disclosure" (in force from 11/05/2007)*

*The Regulations prescribe the procedure of disclosure the information on risks inherent to the Bank, risk management goals, methods and policies, as well as requirements for own funds and internal capital adequacy.*

*The Bank complies with the provisions of the Regulations at individual and consolidated group level.*

## CONSOLIDATION GROUP

JSC „TRASTA KOMERCBANKA” is the Group Holding Company which applies unified requirements for information disclosure at consolidation level. Risk management of the Bank’s Subsidiaries is fully integrated in the risk management process of the Bank.

The Bank has founded two subsidiaries in Latvia, i.e. “TKB LĪZINGS”, Ltd, and “TKB NEKUSTAMIE ĪPAŠUMI”, Ltd, which are consolidated with the Bank according to the full consolidation method and are subject to consolidated supervision:

- TKB Līzings, Ltd (reg. No. 40003591059, Latvia, Riga, Miesnieku Street 9)
- TKB Nekustamie īpašumi, Ltd reg. No. 40003723143, Latvia, Riga, Miesnieku Street 9).

## Consolidation principles

The Bank has consolidated its subsidiaries in the consolidated financial statements in accordance with International Accounting Standard 27. Subsidiaries are the companies controlled by the Bank. The control is applied if the Bank has direct or indirect influence over the company’s financial and activities policy.

The consolidation is based on control over the subsidiaries, which results from the majority of rights to vote in the subsidiaries

When preparing the consolidated financial statements, their items were evaluated in accordance with the uniform accounting policies, which are used by the Group consistently from year to year in conformity with the International Financial Reporting Standards as adopted by European Union and the Financial and Capital Market Commission regulations on preparation of Bank’s financial statements. If any of the accounting policies used by the subsidiaries differ from those applied by the Bank, the financial statements of the subsidiaries are adjusted for consolidation purposes. The financial statements of the subsidiaries were included in the Group’s consolidated financial statements applying the method of full consolidation.

Minority interest is the interest in subsidiaries which is not held, directly or indirectly, by the Bank. Minority interest at the balance sheet date represents the minority shareholders' portion of the fair value of the identifiable assets, liabilities and contingent liabilities of the subsidiary at the acquisition date and the minorities' portion of movements in equity since the date of the consolidation. Minority interest is presented within equity.

Detailed information about the subsidiaries is presented in the Bank’s financial statements for 2009.

## RISK CONTROL AND MANAGEMENT

As the amount of transactions at the Group's level was insignificant, the Bank performs management of the relevant risks individually, except credit risk which is managed at the Group's level. The same procedures that are described below are used for risk management at the Group's level.

### General principles

In order to manage Bank's exposures the Bank identifies on a regular basis the risks inherent to its activities. The Bank regularly assesses the risks that may affect its operation and performance results. For each important exposure the Bank has elaborated appropriate policies and control procedures. For the purpose of management and control of Bank's risks the Bank has approved the Risk Management Policy, Capital Adequacy Assessment Policy, Liquidity Management Policy, Foreign Currency Risk Management Policy, State Risk Management Policy, Lending Policy, Investment Policy, Reputation Risk Management Policy, Compliance Function Risk Management Policy, Policy on Prevention of Money Laundering and Terrorist Financing and other policies, which the Bank Board and Council have approved. These policies are developed according to the Bank's Strategic Plan and they are regularly updated taking account of the development of the market and Bank activities.

These policies define the principles according to which the Bank defines:

- ✓ general guidelines which govern the Bank in its activities in order to minimise all kinds of risks which may result in losses ;
- ✓ classification of risk transactions and other risks to which the Bank is exposed in its operating activities;
- ✓ general day-to-day control and administration of risks of the Bank.

The main purpose of the Risk Management Policy of the Bank is to describe and determine an aggregate of means with help of which the Bank would be able to ultimately minimise any probability of incurring losses in situations where the funds deposited by the Bank or the funds that are due to the Bank are not paid on time and in the full amount, or the Bank incurs losses of another kind.

The Risk Management Policy of the Bank is implemented by the Bank Council, Board, Asset-Liability Assessment Committee (hereinafter – ALCO), Loan Committee, Loan Assessment Committee and respective Bank subdivisions controlling risk transactions.

*The Council* provides general management of the Bank ensuring achievement of the goals and targets set in the Articles of Association. To exercise control over the risk management system of the Bank, the Council approves internal risk management policies, ensures compliance with such policies, their efficiency analysis and improvement.

*The Board* provides day-to-day management of the Bank ensuring compliance with the internal documents which set out the risk management procedures and requirements, distribution of powers and responsibilities among subdivisions and elaboration, approval and submission of risk management reports. The Board ensures identification and management of operational risks.

*ALCO Committee* determines the asset-liability structure of the Bank, sets and monitors parameters controlling balance and off-balance sheet positions - limits for positions of assets and liabilities; where necessary, it sets the volume of special provisions for doubtful loans, save for the portfolio of commercial loans where reserves are set by the Loan Committee; ensures the Bank's ability to fulfil its current financial liabilities, takes charge of long-term liquidity of the Bank by forming a balanced asset-liability term-structure; takes care of ensuring the Bank contingent activities with financial

resources; analyses, assesses and controls risks of the Bank on a regular basis; elaborates and revises regularly limits restricting risks of the Bank; keeps track of compliance with these limits; determines assets/liabilities portfolios of the Bank (commercial loans, interbank loans, securities and others) and their limits; determines administrators of portfolios and guidelines of administration; defines and conducts correspondent banking policy of the Bank; at least once a quarter provides assessment of correspondent banks and state of correspondent accounts.

*Loan Committee* is in charge of elaboration of the Bank Lending Policy; formation of the loan portfolio and its management within the framework of the Lending Policy; considers loan applications and guarantee requests; takes decisions on lending terms and conditions and interest rates of loans to be granted; on a regular basis (at least once a month) inspects the quality of loan portfolio.

*Loan Assessment Committee* develops certain procedures in order to timely identify impairment of loan quality, i.e. main criteria for assessment and classification; revises procedures in place on a regular basis and, where necessary, amend the same regularly but no less than once a quarter, provides assessment of loan quality of the Bank and classification according to the respective risk degree and based on the assessment and classification criteria.

*The AML Compliance Committee* works on a regular basis in order to improve the internal control system for prevention of money laundering and terrorist financing according to the developed and approved plans.

*The Compliance Function Committee* is a unit established in the Bank which is responsible for identification, assessment and management of of compliance risk. Compliance risk is the risk of the Bank to suffer losses or to become subject to legal liabilities or to sanctions, or the risk to deteriorate the bank's reputation due to non-compliance or breach of compliance laws by the Bank.

The main purpose of *the Internal Audit Division* is to provide independent and objective evaluation of effectiveness of the internal control system of the Bank and its monitoring in order to assist the Council and the Board and subdivisions of the Bank to perform their functions with greater efficiency. The Internal Audit Division performs its work in accordance with the activities plan approved by the Council. On every audit performed by the Internal Audit Division it prepares a report to the Bank management of its findings and deficiencies in the internal control system, policies and procedures, and inadequately identified or managed risks and it provides recommendations for remedial actions.

### **Substantial risk inherent to activities of the Bank**

Bank's activities are subject to the following risks:

- [credit risk](#);
- [market risk](#);
- [interest rate risk](#);
- [liquidity risk](#);
- [country risk](#);
- [operational risk](#);
- [concentration risk](#);
- [reputation risk](#);
- [money laundering and terrorism financing risk](#);
- [strategy and business risks](#).

## OWN FUNDS

The Bank's capital adequacy requirements are determined and supervised by the FCMC. According to the capital adequacy requirements set by the FCMC, banks should maintain capital adequacy according to the risk - weighted assets above the set minimum level. As of 31 December 2009, the minimum level was 8%.

The table incorporates information about the compliance with regulatory minimum capital adequacy requirements and own funds elements in 2009 (in thousands of lats):

	<u>Grupa</u> <u>2009</u>	<u>Banka</u> <u>2009</u>
<b>OWN FUNDS</b>	<b>32 293</b>	<b>32 724</b>
<b>Tier 1 capital</b>	<b>31 933</b>	<b>32 364</b>
<b>Adequate equity</b>	<b>6 448</b>	<b>6 448</b>
Paid up capital	6 337	6 337
Share issue premium	111	111
<b>Adequate reserves</b>	<b>25 758</b>	<b>26 188</b>
Reserve capital and other reserves, revaluation reserves and retained profit and losses of previous years	27 398	28 181
Minority interest	9	-
Audited profit of the current year of operation or audited (losses) of the current year of operation	(1 628)	(1 972)
Revaluation reserves relevant to Tier 1 capital and changes in fair value	-	-
Revaluation reserve for other available for sale financial assets	(21)	(21)
<b>Other elements reducing Tier 1 capital (-)</b>	<b>(273)</b>	<b>(272)</b>
Intangible assets	(273)	(272)
<b>Tier 2 capital</b>	<b>3 717</b>	<b>3 717</b>
<b>2 group of Tier two capital</b>	<b>3 717</b>	<b>3 717</b>
Subordinated capital	3 717	3 717
<b>Deductions from Tier 1 and Tier 2 capital</b>	<b>(3 357)</b>	<b>(3 357)</b>
Deductions from Tier 1 and Tier 2 capital prescribed by the legislation <sup>1</sup>	(3 357)	(3 357)
<b>SUMMARY OF CAPITAL REQUIREMENT CALCULATIONS</b>	<b>17 896</b>	<b>17 363</b>
<b>Total of capital requirements for credit risk, counterparty credit risk, dilution risk and free deliveries risk according to standardized approach</b>	<b>13 384</b>	<b>13 545</b>
Public authorities	47	47
Institutions	1 944	1 944
Commercial companies	6 804	6 984
Secured by real property	144	144
Delayed exposures	2 058	2 035
Other items	2 387	2 391
<b>Capital requirements for position, foreign exchange and commodities risks according to standardized approach</b>	<b>386</b>	<b>336</b>
Traded debt instruments	114	114
Equity instruments	110	110
Foreign currency	162	112

<i>Capital requirements for operational risk according to basic indicator approach</i>	4 126	3 482
<b>CAPITAL REQUIREMENTS COVERED BY OWN FUNDS (SUPLUS (+) OR SHORTFALL (-))</b>	<b>14 397</b>	<b>15 361</b>
<b>CAPITAL ADEQUACY RATIO (%)</b>	<b>14.44</b>	<b>15.08</b>

<sup>1</sup> According to the assessment of the Financial and Capital Market Commission, the Bank has to make additional provisions in the amounts of 3 357 thousand lats.

### CAPITAL ADEQUACY ASSESSMENT PROCESS

For the purpose of capital adequacy assessment and in accordance with its capital adequacy maintenance strategy the Bank has defined that capital is an aggregate of elements of capital, reserves and liabilities which are freely available to the Bank to cover contingent, yet not identified, losses related to risks of ordinary activities. To assess capital adequacy the Bank applies the "First Pillar+" approach using as a basis the regulatory minimum capital requirements, set in the amount of 8% of the total of their risk-weighted exposure amounts, and including the following risks and assessment methods:

- ✓ for credit risk capital requirements – *standardised approach*;
- ✓ for market risk capital requirements - *standardised approach*;
- ✓ for operational risk capital requirements – *key figure approach*.

Within the framework of the internal capital adequacy assessment the Bank:

- ✓ evaluates whether the calculated regulatory minimum capital requirements for credit risk, operational risk and market risk are adequate and comply with the Bank's activities;
- ✓ assesses the risks for which the regulatory minimum capital requirements are not set and calculates the amount of capital that is necessary to cover the substantial risks;
- ✓ determines the reserve of capital;
- ✓ determines the amount of internal capital that is necessary to cover overall risks;

In addition to the obligatory regulatory minimum capital requirements for covering of credit risk, market risk and operational risk, the Bank maintains additional reserves to cover the following substantial risks:

- ✓ concentration risks (loan portfolio concentration, claims on credit institutions concentration, incl. by countries);
- ✓ Money laundering and terrorism financing risks (AML);
- ✓ reputation risk,
- ✓ strategy and business risks.

In determining the amount of the capital required for covering the substantial risks, the Bank recognizes the diversification effect of risks. To determine the diversification effect the Bank applies the "constant diversification" method offered in Basel – II document "Range of practices and issues in economic capital modeling"

Upon assessment of the internal capital adequacy for 2009, the Bank has determined the internal capital adequacy level not less than 10%.

The analysis of the actual figure of Bank's capital in the reporting year is provided in the table below:

	<u>2009</u>
	%
31 December	15.08
Average for the period	16.55
Highest level	17.52
Lowest level	14.83

The Bank performs assessment of the internal capital adequacy on a regular basis, but at least once a year. Capital planning takes place during the budget preparation process. In the budget preparation process the Bank develops the capital increment plan whose sources are as follows:

- ✓ increase of the capital through share issue;
- ✓ attraction of subordinated capital;
- ✓ formation of operation development reserves from profit of the Bank;
- ✓ retained earnings from the previous year;
- ✓ audited profit of the current year (by permission of the Financial and Capital Market Commission).

The Bank has prepared a contingency plan to maintain its capital adequacy in case of threat for the capital adequacy ratio to fall under the established standard. In addition to the above described capital increasing sources, the plan foresees:

- ✓ improvement of asset quality;
- ✓ asset restructuring for the purpose of minimising the share of risk group assets;
- ✓ application of Tier 3 capital elements (by permission of the Financial and Capital Market Commission).

The Bank management ensures daily supervision of the capital adequacy. The relevant subdivisions regularly provide information to the ALCO Committee and the Board on compliance with the internal capital adequacy level and minimum regulatory requirements, as well as capital adequacy scenario analysis. The Board at least once a year submits a report to the Council on the state of capital.

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