AAS BALTA

Annual Report for 2017 prepared in accordance
with the International Financial Reporting Standards
as adopted by the European Union and
Independent Auditors' Report

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Information on the Company, Members of the Supervisory Board and the Management Board, Independent Auditors

Information on the Company

Name of the Company	Insurance Joint Stock Company BALTA
Legal address of the Company	10 Raunas Street, Riga, LV-1039, Latvia
Number and date of registration	40003049409, registered on 28 January 1992, re-registered in the Commercial Register of the Republic of Latvia on 6 June 2002

Supervisory Board

Name, Surname	*Position*
Roger Hilton Hodgkiss	Member of the Supervisory Board (from 18.08.2017 until 20.10.2017) Chairman of the Supervisory Board (from 20.10.2017; reappointed on 18.01.2018)
Lidia Maria Orzechowska	Member of the Supervisory Board (from 18.08.2017 until 20.10.2017) Deputy of the Chairman of the Supervisory Board (from 20.10.2017; reappointed on 18.01.2018)
Katarzyna Anna Galus	Member of the Supervisory Board (from 18.01.2018)
Anna Teresa Mank	Member of the Supervisory Board (from 18.01.2018)
Pawel Karol Zacharkiewicz	Member of the Supervisory Board (form 18.08.2017; reappointed on 18.01.2018)
Maciej Bogdan Rapkiewicz	Chairman of the Supervisory Board (until 23.03.2017); Member of the Supervisory Board (from 23.03.2017; reappointed on 18.08.2017; resigned on 31.12.2017)
Piotr Józef Kruszyński	Member of the Supervisory Board (reappointed on 23.03.2017 until 07.07.2017)
Tomasz Edward Czuba	Member of the Supervisory Board (reappointed on 23.03.2017 until 07.07.2017)
Wacław Wojciech Szary	Member of the Supervisory Board (reappointed on 23.03.2017 until 07.07.2017)
Krzysztof Mariusz Markowski	Member of the Supervisory Board (reappointed on 23.03.2017 until 07.07.2017)
Agnieszka Ewa Karbowiak	Chairman of the Supervisory Board (from 23.05.2017 until 07.07.2017); Member of the Supervisory Board (from 23.03.2017 until 23.05.2017)
Jacek Adrian Matusiak	Member of the Supervisory Board (from 23.03.2017; until 24.04.2017)

Management Board

Name, Surname	*Position*
Iain Kennedy	Chairman of the Management Board (from 16.08.2017)
Bogdan Benczak	Chairman of the Management Board (until 19.05.2017)
Rafal Piotr Rybkowski	Management Board Member
Ingus Savickis	Management Board Member (reappointed on 24.08.2017)
Uldis Dzintars	Management Board Member
Mārtiņš Rozentāls	Management Board Member
Malgorzata Krystyna Piotrowska	Management Board Member
Marcin Tomasz Majerowski	Management Board Member

Name and address of the independent auditors and responsible Latvian certified auditor:

KPMG Baltics SIA	Responsible Latvian certified auditor:
Licence No. 55	Inga Lipšāne
Vesetas iela 7, Riga,	Latvian certified auditor
LV-1013, Latvia	Certificate No. 112

Report of the Supervisory Board and the Management Board

Main developments

According to market data provided by Latvian Insurers Association and Financial and Capital Market Commission, as well as insurance company public quarterly reports in 2017, BALTA (hereinafter – "Company") has been able to maintain its leading position as the largest company in the Latvian non-life insurance market in terms of gross premiums written in Latvia. Significant business growth and developing operational excellence, have resulted in gross written premiums of 88.9 million EUR and total comprehensive income of 6.4 million EUR for 2017. The continuous profitability has secured also the financial stability of the Company – the Solvency II ratio as at the end of the year is well above the minimum requirements set by Financial and Capital Market Commission of the Republic of Latvia

According to data from Latvian Insurers Association, in 2017 BALTA managed to grow in line with the Latvian non-life insurance market by increasing gross written premiums by 13 million EUR or 18% compared to 2016, which resulted in market share of 28%. The Company has managed to grow all its significant portfolios; the majority of them above the market growth level. In 2017, BALTA has managed to conclude several new partnerships to widen the Company's distribution network.

The wide range of insurance products and focus on exploring and meeting customer needs enabled BALTA to retain a leading position in the market not only by volume, but also by customer recognition. According to the results of an independent survey of insurance companies in Latvia, carried out by LETA and SKDS in 2017, BALTA was recognized as the country's most honest insurer for the 15th year. In 2017, BALTA was recognized as "Most Loved Insurance Company" in Latvia in independent research carried out by DDB and Kapitāls while Ministry of Welfare of Latvia awarded BALTA as "Family Friendly Company" and in Sustainability Index 2017 (InCSR) Company qualified for Gold category – the only insurance company in Latvia receiving so high evaluation. According to the results of a survey of „Aon Best Employers" in 2017, BALTA was recognized as one of the Best Employers in Baltics for the third time.

Strong performance of BALTA brand and reputation is also seen in annual BALTA brand research – Top of Mind indicator is 34%, while Total awareness has increased to 92%. From customers point of view, BALTA is recognized for positive collaboration experience, good deal and price offers. BALTA Reputation score among those who know the company is evaluated as 8.1 out of 10. BALTA is continuously evaluated as market leader among insurance companies in terms of awareness, TOP choice and consideration, as well as usage of insurance companies.

Both the financial performance and the Company's customer focus, supported by an excellent external and customer recognition in the Latvian market, ensures BALTA a leading position in the Latvian insurance market and gives it a strong platform for further growth and development.

Insurance market in 2017

Insurance industry experienced a relatively calm period for several years, however, year 2017 has been the most dynamic in recent decade resulting in significant market development. Non-life insurance market growth has increased to 18%, which is three times faster than in previous years. Growth is driven mainly by price increases in motor insurance segment, higher economy growth (especially construction industry) and increased number of customers. High insurance market growth rates are observed also in other Baltic countries. However Baltics' insurance penetration in the overall economy is still below the European average level.

Business growth is accompanied by increased claims inflation for major business lines, and this trend is expected to continue in the coming period. Despite increase in prices, the MTPL portfolio is still not profitable due to a sharp increase in claims costs and deferred recognition of earned premiums in accordance with policies cover periods. Motor insurance market has also experienced increase of losses due to car thefts, where a significant increase in stolen new cars has happened. Many insurers have responded by compulsory requirement of theft prevention systems in high risk segments.

In accordance with the Financial and Capital Market Commission of the Republic of Latvia data, the Latvian domestic non-life insurance market has not gained profit from insurance activities since 2011 (there is still some profit from investment activities). The latest data shows that insurers' profitability results have improved in 2017 and the combined ratio was approximately 95% in the 3rd quarter of 2017, while in previous years it was over 100%.

Risk management

Risk Management System supports the BALTA's Internal Control System and System of Governance. The Company's business strategy has ensured establishment of integrated, consistent and effective risk management system, reflecting the Company's size, scope and complexity. The risk management process consists of identification, measurement and assessment, monitoring and control, reporting and management actions. Identification starts with the idea of creating an insurance product, acquiring a financial instrument or changing an operating process, as well as at the point, when any other event takes place which could potentially create a risk. Once identified, all risks are measured and assessed based on capital need or other quantitative or qualitative assessment criteria, both on at individual and at an aggregated level. Each identified risk is a subject to monitoring and control. The method is proportionate to the nature, scale and complexity of this risk. Risk management actions are taken by operational units (first line of defense), the key functions (risk management function, actuarial function, compliance function and financial controlling function), Committees (in particular Risk Committee that considers the latest trends in risk development and changes to the risk appetite, risk profile, risk tolerance limits and other indicators of the material risks and assesses the impact of each of these changes and documents new risks identified in all operational areas of the Company) and the Management Board ensuring that risk levels have not exposed the Company to excessive level of risks determined by the Company.

Capital adequacy and solvency are under constant focus of BALTA. At the end of 2017, the capital of BALTA exceeded the capital required according to law and the rules of the Financial and Capital Market Commission of the Republic of Latvia. Stress tests are performed by BALTA within Own Risk and Solvency assessment process to assess the impact of a number of adverse insurance and financial risks on the Company's solvency. It was demonstrated by modelling of several adverse scenarios that capital adequacy and solvency of BALTA was sufficient and the Company would be able to meet its liabilities towards customers and retain its financial stability also under unexpected adverse scenarios.

Customer service and payment of claims

In 2017, BALTA continued to improve the process of monthly customer feedback gathering and analysis as well as implementing several system improvements enabling the Company to introduce new customer oriented initiatives and improve customer service.

All customer feedback was analyzed on individual level and specific suggestions received from customers regarding insurance and servicing were delivered to sales persons with the aim to improve BALTA cooperation with customers also on individual level. Along NPS (Net Promoter Score) surveys by phone, also automated NPS survey by mail after receiving claim payments is implemented with the aim of getting customer feedback and evaluating the whole claim handling process. Customers particularly appreciate easy and quick policy purchase process and understandable insurance products, therefore, in 2017, BALTA started the implementation of a simplified property insurance product for flats (easy to buy on the internet with a few clicks and answering a few questions; automated monthly payments are available). Web solution and design for purchase of Travel and MOD insurance has been improved.

BALTA continued to maintain high quality and convenient claim handling service – development of web solutions for claim handling led to more simplified, convenient and efficient claims notifications for customers. These solutions have also resulted in shorter period needed for claims decisions. Customers of BALTA appreciate the speed and convenience of claims handling. Several activities were implemented in 2017 such as:

- Improved information to customers in claim letters;
- Notification system about the claim handling process (responsible person, decision terms, etc.) by SMS has been improved;
- Several improvements for entering MOD claims into web system have been done (easier and faster for the client to apply for a compensation);
- Design and web solution for application form for health claim has been improved (customers now can apply for a health compensation also from mobile devices; data filling process is made easier and more convenient for the customer);
- A new web solution for registration of purchase insurance related claims was launched. In the nearest future similar solutions will be launched also for travel and other insurance products.

One of the largest initiatives launched in 2017 is a project regarding the Customer facing documentation review including Customer communication strategy development.

Working environment in the Company and professional development of staff

In 2017, BALTA continued the implementation of people strategy. Similarly to the year before, BALTA was focused on raising employee engagement, mainly by improving development opportunities as well as physical working environment. Special attention was given to the development of new managers. There have been a number of training activities also for specialist level employees in order to increase sales skills, business knowledge and collaboration, raise aspirations and increase personal efficiency.

BALTA continued the Work and Life Balance program, which supports employees with long service in the Company by assigning additional holidays, providing special support for mothers of young children and special benefit packages for employees with children, greetings to employees on important occasions etc.

Our efforts in work with employees resulted with both internal and external recognition. Internally, we managed to improve employee engagement by 6 percentage points reaching 79% and reduced employee turnover by more than 4 percentage points.

Externally, we received an award as a Family Friendly enterprise given by Ministry of Welfare of Republic of Latvia (second year in row), as well as 2nd place in Latvian Labor Inspection contest about integration of employees after long term absence.

Report of the Supervisory Board and the Management Board

Corporate social responsibility

BALTA takes care about Corporate Social Responsibility (CSR), and the ambition of the Company is to be an active and responsible member of the Latvian society. BALTA's social support principles and priority social support fields are set in the AAS BALTA Corporate responsibility policy and the AAS BALTA Community support policy, and for 2017 they were – security, local community (education, culture, financial literacy, health) and the environment. 2017's social support activities included sponsorships, donations and gifts, volunteer work and strategic project initiatives with the overall goal of promoting positive change in the local community. Few of the biggest CSR initiatives carried out in 2017: BALTA annual award "Safest Business Car Park" – a contest for businesses with the goal of promoting the education of car park managers and overall traffic safety; project "Have Fun Safely", where the goal is to remind and educate the society about safe leisure time at swimming spots and near water; participation in the Latvian State Police campaign "Superheroes Don't Get Lost" with the goal of promoting child safety issues and other. An important part of social support is also education – for many years BALTA has been financing a scholarship program for the BA School of Business and Finance Risk Management students, financially supporting the new specialists of this sector. In addition, BALTA regularly collaborates with education institutions, familiarizing schoolchildren and students with the essentials of the insurance sector and taking part in career and shadowing day activities. BALTA CSR initiatives and activities are also communicated daily through the media and social networks.

Additionally to that, as one of BALTA's core values is honesty, a lot of attention is paid to responsible attitude towards customers and partners in insurance sales process. To be in line with this value regular trainings are organized for all stakeholders – insurance agents, sales partners and brokers – about insurance services offered by BALTA and responsible attitude towards customers.

BALTA's investments in society, as well as an ethical and honorable attitude towards customers and business partners, is recognized also by independent experts and society as a whole. Every year BALTA takes part in the strategic management tool "Sustainability index - InCSR," which gives the business the opportunity to receive evaluation and suggestions of independent experts. In 2017, in the Sustainability index BALTA qualified for Gold category award – the total result marked by independent experts was 87.6%, while the average mark in the financial and insurance sector was only 68.3%. Additionally to that, BALTA already for several years is part of Society Integration Foundation of Latvia project "Goda ģimene" providing discounts for insurance services to families with three and more children, while every Christmas support is provided to children from orphanages. These activities have been recognized also by the Ministry of the Welfare of Latvia by awarding BALTA as Family Friendly Company.

Proposals regarding distribution of the Company's profit

In accordance with the Company Dividend policy, the Supervisory Board and Management Board of BALTA do not recommend the payment of dividends in 2018.

Subsequent events

No events have taken place from the Statement of Financial Position date to the date of approval of these financial statements that could materially affect the annual performance, cash flows or the financial position or related disclosures of BALTA as at and for the year ended on the reporting date.

In the extraordinary Shareholders` meeting on 8 November 2017 the current Supervisory Board members of BALTA where elected. The changes have been registered in the Commercial Register of the Republic of Latvia as at 18 January 2018.

Roger Hilton Hodgkiss
Chairman of the Supervisory Board

Iain Kennedy
Chairman of the Management Board

16 March 2018

Statement of the Supervisory Board's and the Management Board's Responsibility

The Supervisory Board and the Management Board of AAS BALTA confirm that the financial statements for the year ended 31 December 2017 are prepared in accordance with the International Financial Reporting Standards as adopted by the European Union and that appropriate accounting policies have been applied on a consistent basis. The Supervisory Board and the Management Board of AAS BALTA are responsible for preparing these financial statements from the books of primary entry. The Supervisory Board and the Management Board confirm that these financial statements for the year ended 31 December 2017 present fairly the financial position of AAS BALTA at the end of the reporting year, and the results of its operations and cash flows for the reporting year.

Prudent and reasonable judgments and estimates have been made by the Supervisory Board and the Management Board in the preparation of the financial statements for the year ended 31 December 2017.

The Supervisory Board and the Management Board of AAS BALTA are responsible for the maintenance of proper accounting records, the safeguarding of the Company's assets and the prevention and detection of fraud and other irregularities in the Company. They are also responsible for operating the Company in compliance with the legislation of the Republic of Latvia.

Roger Hilton Hodgkiss	Iain Kennedy
Chairman of the Supervisory Board	Chairman of the Management Board

16 March 2018

Financial statements
Statement of Comprehensive Income *(All amounts in euros)*

	Exhibit	2017	2016
Insurance income			
Gross written premiums	4	88 921 657	75 610 261
Reinsurer's share in written premiums	4	(3 027 986)	(2 432 335)
Net written premiums	4	85 893 671	73 177 926
Change in gross unearned premium reserves	5	(6 790 026)	(3 712 350)
Change in unearned premium reserves, reinsurers' share	5	330 504	164 411
Change in unearned premium reserves	5	(6 459 522)	(3 547 939)
Net premiums earned		**79 434 149**	**69 629 987**
Other technical income	6	359 245	354 046
Total insurance income		**79 793 394**	**69 984 033**
Insurance expenses			
Gross claims paid to policyholders		(47 275 961)	(44 357 938)
Loss adjustment expenses		(3 539 626)	(3 196 334)
Recovered losses		3 886 405	3 083 873
Claims paid	7	(46 929 182)	(44 470 399)
Reinsurer's share in claims paid	7	1 252 298	3 203 801
Net claims paid		(45 676 884)	(41 266 598)
Change in gross outstanding claims reserves	8	(3 903 185)	1 148 845
Change in outstanding claims reserves, reinsurers' share	8	1 474 386	(2 250 779)
Net incurred claims		**(48 105 683)**	**(42 368 532)**
Client acquisition costs	9	(13 175 290)	(12 392 496)
Administrative expenses	10	(12 091 921)	(10 974 270)
Other technical expenses	11	(466)	(19 502)
Total insurance expenses		**(73 373 360)**	**(65 754 800)**
Net result of insurance activities		**6 420 034**	**4 229 233**
Interest income	12	1 688 321	1 291 764
Net profit / (loss) on financial assets	13	(1 021 146)	(447 308)
Investment management expenses		(170 390)	(236 998)
Other finance income	14	302	210
Other finance expenses	15	(133 330)	(130 541)
Other income	16	60 587	28 270
Other expenses	17	(14 162)	(3 669)
Profit before tax		**6 830 216**	**4 730 961**
Changes in deferred income tax asset	18, 26	(284 850)	(705 943)
Corporate income tax for the reporting year		(619 806)	-
Profit for the year		**5 925 560**	**4 025 018**
Other comprehensive income			
Items that are or may be reclassified to profit or loss			
Change in revaluation reserve	23	475 669	58 281
Deferred tax effect from changes in revaluation reserve	23, 26	8 742	(8 742)
		484 411	**49 539**
Other comprehensive income for the period, net of tax		**484 411**	**49 539**
Total comprehensive income for the reporting year		**6 409 971**	**4 074 557**

All profit is attributable to the owners of AAS BALTA.

Notes on pages 13 to 49 are an integral part of these financial statements.

Roger Hilton Hodgkiss
Chairman of the Supervisory Board

Iain Kennedy
Chairman of the Management Board

16 March 2018

Statement of Financial Position *(All amounts in euros)*

	Exhibit	31.12.2017	31.12.2016 (restated*)
ASSETS			
Intangible assets	19	**2 021 702**	**1 967 600**
Property and equipment	20	**2 893 345**	**2 845 326**
Financial investments at fair value through profit or loss	21	11 007 477	14 975 767
Held to maturity financial investments	22	21 887 193	22 873 783
Available for sale financial investments	23	34 363 484	14 735 714
Total investments		**67 258 154**	**52 585 264**
Receivables due from policyholders		14 486 850	12 416 574
Receivables due from intermediaries		1 003 742	649 271
Receivables from direct insurance operations	24	15 490 592	13 065 845
Reinsurance receivables	25	532 913	217 591
Other receivables	28	935 082	901 064
Total receivables		**16 958 587**	**14 184 500**
Reinsurers' share in unearned premium reserves	5	1 146 350	815 846
Reinsurers' share in outstanding claims reserves	8	4 437 779	2 963 393
Reinsurers' share of insurance contract liabilities		**5 584 129**	**3 779 239**
Deferred income tax asset	26	**-**	**276 108**
Deferred client acquisition costs	9	9 219 959	8 071 028
Other accrued income and deferred expenses	27	747 406	424 522
Accrued income and deferred expenses		**9 967 365**	**8 495 550**
Cash and cash equivalents	29	**4 111 878**	**8 688 012**
TOTAL ASSETS		**108 795 160**	**92 821 599**

Notes on pages 13 to 49 are an integral part of these financial statements.

* For information on the restatement refer to Note 24.

Roger Hilton Hodgkiss
Chairman of the Supervisory Board

Iain Kennedy
Chairman of the Managment Board

16 March 2018

Statement of Financial Position *(All amounts in euros)*

	Exhibit	31.12.2017	31.12.2016 (restated*)
SHAREHOLDERS' EQUITY, RESERVES AND LIABILITIES			
SHAREHOLDERS' EQUITY AND RESERVES			
Share capital	30	6 619 290	6 619 290
Share premium	30	1 595 511	1 595 511
Reserve capital and other reserves	30	4 357 130	4 357 130
Revaluation reserve		533 950	49 539
Retained earnings		13 496 438	9 603 946
TOTAL SHAREHOLDERS' EQUITY AND RESERVES		**26 602 319**	**22 225 416**
LIABILITIES			
Gross unearned premium reserves	5	42 981 501	36 191 475
Gross outstanding claims reserves	8	26 361 933	22 458 748
Insurance contract liabilities		**69 343 434**	**58 650 223**
Subordinated loan	37	2 085 828	4 173 022
Direct insurance creditors		4 488 477	3 018 509
Reinsurance creditors		1 000 212	793 548
Taxes and the state compulsory social insurance contributions	31	1 149 678	481 142
Accrued expenses and deferred income	32	3 129 018	2 513 629
Other creditors	33	996 194	966 110
Total creditors		**12 849 407**	**11 945 960**
TOTAL LIABILITIES		**82 192 841**	**70 596 183**
TOTAL SHAREHOLDERS' EQUITY, RESERVES AND LIABILITIES		**108 795 160**	**92 821 599**

Notes on pages 13 to 49 are an integral part of these financial statements.

* For information on the restatement refer to Note 24.

Roger Hilton Hodgkiss
Chairman of the Supervisory Board

Iain Kennedy
Chairman of the Management Board

16 March 2018

Statement of Changes in Shareholders' Equity *(All amounts in euros)*

	Share capital	Share premium	Reserve capital and other reserves	Revaluation reserve	Retained earnings	Total
Balance at 31 December 2015	**6 619 290**	**1 595 511**	**4 357 130**	**-**	**5 578 928**	**18 150 859**
Total comprehensive income for the year	**-**	**-**	**-**	**49 539**	**4 025 018**	**4 074 557**
Profit for the year	-	-	-	-	4 025 018	4 025 018
Other comprehensive income	**-**	**-**	**-**	**49 539**	**-**	**49 539**
Net change in revaluation reserve, net of deferred tax effect	-	-	-	49 539	-	49 539
Balance at 31 December 2016	**6 619 290**	**1 595 511**	**4 357 130**	**49 539**	**9 603 946**	**22 225 416**
Total comprehensive income for the year	**-**	**-**	**-**	**484 411**	**5 925 560**	**6 409 971**
Profit for the year	-	-	-	-	5 925 560	5 925 560
Other comprehensive income	**-**	**-**	**-**	**484 411**	**-**	**484 411**
Net change in revaluation reserve, net of deferred tax effect	-	-	-	484 411	-	484 411
Transactions with the owners of the Company	**-**	**-**	**-**	**-**	**(2 033 068)**	**(2 033 068)**
Distributed dividends	-	-	-	-	(2 033 068)	(2 033 068)
Balance at 31 December 2017	**6 619 290**	**1 595 511**	**4 357 130**	**533 950**	**13 496 438**	**26 602 319**

Notes on pages 13 to 49 are an integral part of these financial statements.

Roger Hilton Hodgkiss
Chairman of the Supervisory Board

Iain Kennedy
Chairman of the Management Board

16 March 2018

Statement of Cash Flows *(All amounts in euros)*

	Exhibit	2017	2016
Cash flows from operating activities			
Premiums received from direct insurance		86 835 247	74 435 153
Claims paid for direct insurance		(46 596 409)	(44 257 484)
Payments received from ceded reinsurance		447 402	3 132 089
Payments made for ceded reinsurance		(1 971 682)	(1 972 173)
Mandatory payments	35	(892 938)	(634 256)
Other expenses		(23 498 910)	(23 054 973)
Net cash from operating activities:		**14 322 710**	**7 648 356**
Cash flows from investing activities			
Disposal of investments		4 282 957	7 384 218
Acquisition of investments		(19 286 147)	(12 358 244)
Purchase of property and equipment and intangible assets		(1 198 684)	(1 045 872)
Proceeds from sale of property and equipment and intangible assets		35 998	-
Interest received from debt securities		1 614 019	1 275 346
Other expenses		(99 372)	(80 669)
Net cash used in investing activities:		**(14 651 229)**	**(4 825 221)**
Cash flows from financing activities			
Repayment of subordinated loan		(2 050 000)	-
Interest paid for subordinated loan		(158 754)	(135 505)
Dividends paid		(2 032 978)	-
Net cash used in financing activities:		**(4 241 732)**	**(135 505)**
Result of foreign exchange rate fluctuations on cash and cash equivalents		**(5 883)**	**(1 590)**
Net increase / (decrease) in cash and cash equivalents		**(4 576 134)**	**2 686 040**
Cash and cash equivalents at the beginning of reporting year		8 688 012	6 001 972
Cash and cash equivalents at the end of reporting year	29	**4 111 878**	**8 688 012**

Notes on pages 12 to 49 are an integral part of these financial statements.

Roger Hilton Hodgkiss
Chairman of the Supervisory Board

Iain Kennedy
Chairman of the Managment Board

16 March 2018

NOTES TO THE FINANCIAL STATEMENTS

1. GENERAL INFORMATION

AAS BALTA (hereinafter "the Company") is an insurance joint stock company which was registered in Riga, the Republic of Latvia in 1992. The Company was re-registered with the Commercial Register on 6 June 2002. The Company offers a wide range of non-life insurance services both to corporate clients and individuals. The Company has received licences in all non-life insurance types, in which it provides services. The licences have been issued by Financial and Capital Market Commission of the Republic of Latvia from 1996 to 1999 and re-registered in 2002.

Name of the Company:	Insurance Joint Stock Company BALTA
Legal address of the Company:	10 Raunas Street, Riga, LV-1039, Latvia
Phone, fax:	(+371) 6708 2333, (+371) 6708 2345
Tax payer's code:	LV40003049409
State Revenue Service department:	Department of large tax payers
Majority shareholder:	POWSZECHNY ZAKŁAD UBEZPIECZEŃ S.A., a joint-stock company, Poland (99.99%)

The Company's shares are not listed. The Company belongs to a group whose parent company trades its shares on the Warsaw Stock Exchange and whose main shareholder is the State Treasury of Poland owning more than 34% of the shares.

2. BASIS OF PRESENTATION OF THE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these financial statements are set out below. Consistent accounting principles have been applied to the financial years presented in these financial statements, except as described below (Notes 2.2.3 and 2.2.4).

2.1 Basis of preparation

2.1.1 Statement of Compliance

These financial statements were prepared in accordance with International Financial Reporting Standards (hereinafter "IFRS") as adopted by the European Union (hereinafter "EU") and in accordance with the regulations issued by Financial and Capital Market Commission of the Republic of Latvia (hereinafter "FCMC") applicable to insurance companies.

These financial statements have been authorised for issue by the Management Board on 16 March 2018. The shareholders have the power to reject the financial statements prepared and issued by management and the right to request that new financial statements be issued.

2.1.2 Functional and Presentation Currency

All amounts in the financial statements are shown in euro (EUR), the Company's functional currency, unless otherwise stated.

2.1.3 Basis of measurement

The financial statements have been prepared on the historical cost basis except for the following captions that are stated at fair value: financial instruments carried at fair value through profit or loss and available-for-sale instruments.

2.1.4 Reporting year

The reporting period comprises the 12 months from 1 January 2017 to 31 December 2017.

2.1.5 Estimates

The preparation of financial statements in conformity with IFRS as adopted by the EU requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Company's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where estimates and judgments are significant to the financial statements are disclosed in Note 3.

2.2 New standards and interpretations, reclassification of balances in the financial statements and changes in accounting policies

2.2.1 Standards and interpretations effective in the reporting period

The Company has adopted the following new standards and amendments to standards, including any consequential amendments to other standards, with the date of initial application of 1 January 2017.

(i) Amendments to IAS 7: Statement of Cash Flows

The amendments require new disclosures that help the users of the financial statements to evaluate changes in liabilities arising from financing activities, including changes from cash flows and non-cash changes (such as the effect of foreign exchange gains or losses, changes arising for obtaining or losing control of subsidiaries, changes in fair value). In line with these new amendments, the Company has disclosed additional information in the financial statements (refer to Note 37).

The following guidance with effective date of 1 January 2017 did not have any impact on these financial statements:

(ii) Amendments to IAS 12 Income Taxes: Recognition of Deferred Tax Assets for Unrealised Losses

(iii) Annual Improvements to IFRSs

2.2.2 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 2017, and have not been applied in preparing these financial statements.

(i) IFRS 9 Financial Instruments (2014) (effective for annual periods beginning on or after 1 January 2018)

This Standard replaces IAS 39, Financial Instruments: Recognition and Measurement, except that the IAS 39 exception for a fair value hedge of an interest rate exposure of a portfolio of financial assets or financial liabilities continues to apply, and entities have an accounting policy choice between applying the hedge accounting requirements of IFRS 9 or continuing to apply the existing hedge accounting requirements in IAS 39 for all hedge accounting.

Although the permissible measurement bases for financial assets – amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit and loss (FVTPL) – are similar to IAS 39, the criteria for classification into the appropriate measurement category are significantly different.

A financial asset is measured at amortized cost if the following two conditions are met:

- the assets is held within a business model whose objective is to hold assets in order to collect contractual cash flows; and,
- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal outstanding.

In addition, for a non-trading equity instrument, a company may elect to irrevocably present subsequent changes in fair value (including foreign exchange gains and losses) in OCI. These are not reclassified to profit or loss under any circumstances.

For debt instruments measured at FVOCI, interest revenue, expected credit losses and foreign exchange gains and losses are recognised in profit or loss in the same manner as for amortised cost assets. Other gains and losses are recognised in OCI and are reclassified to profit or loss on derecognition.

The impairment model in IFRS 9 replaces the ‘incurred loss’ model in IAS 39 with an ‘expected credit loss’ model, which means that a loss event will no longer need to occur before an impairment allowance is recognised.

IFRS 9 includes a new general hedge accounting model, which aligns hedge accounting more closely with risk management. The types of hedging relationships – fair value, cash flow and foreign operation net investment – remain unchanged, but additional judgment will be required.

The standard contains new requirements to achieve, continue and discontinue hedge accounting and allows additional exposures to be designated as hedged items.

Extensive additional disclosures regarding an entity’s risk management and hedging activities are required.

It is expected that the new Standard, when initially applied, will have a significant impact on the financial statements, since the classification and the measurement of the Entity’s financial instruments are expected to change.

The Company, as an insurance provider, is entitled to postpone the implementation of IFRS 9 standard until 1 January 2021, however, as PZU Group, to which the Company belongs to, is not allowed to exercise this exemption due to a significant share of banking activity in the Group, BALTA will not apply the exemption from adopting IFRS 9 and plans to adopt it as of 1 January 2018 together with other Group companies. The IFRS 9 implementation project in the Group is managed by the Company’s parent company PZU S.A.

The Company is in the final stage of the IFRS 9 implementation impact assessment. As the Company’s receivables are mostly short-term, the Company does not estimate a significant impact from the calculation of loss allowances for receivables according to IFRS 9. Based on the investment ratings of the Company's investments in debt securities, the Company does not estimate a significant impact from the calculation of loss allowances for investments in debt securities according to IFRS 9. EUR 21 887 thousand of investments are estimated to be reclassified out of held-to-maturity (IAS 39 classification) to fair value through other comprehensive income (IFRS 9 classification). EUR 8 919 thousand of investments are estimated to be reclassified out of financial instruments at fair value through profit or loss (IAS 39 classification) to fair value through other comprehensive income (IFRS 9 classification). EUR 34 363 thousand of available for sale investments (IAS 39 classification) are estimated to retain fair value through other comprehensive income classification under IFRS 9. EUR 2 089 thousand of financial instruments at fair value through profit or loss (IAS 39 classification) are estimated to retain fair value through profit or loss classification under IFRS 9. The estimated impact on classification and measurement is a market re-valuation of EUR 660 thousand, which will lead to an increase in the shareholders' equity.

(ii) IFRS 15 Revenue from contracts with customers (effective for annual periods beginning on or after 1 January 2018)

This Standard provides a framework that replaces existing revenue recognition guidance in IFRS. Entities will adopt a five-step model to determine when to recognise revenue, and at what amount. The new model specifies that revenue should be recognised when (or as) an entity transfers control of goods or services to a customer at the amount to which the entity expects to be entitled. Depending on whether certain criteria are met, revenue is recognised:

- over time, in a manner that depicts the entity's performance; or
- at a point in time, when control of the goods or services is transferred to the customer.

IFRS 15 also establishes the principles that an entity shall apply to provide qualitative and quantitative disclosures which provide useful information to users of financial statements about the nature, amount, timing, and uncertainty of revenue and cash flows arising from a contract with a customer.

Although it has not yet fully completed its initial assessment of the potential impact of IFRS 15 on the Company's financial statements, the Company management does not expect that the new standard, when initially applied, will have a material impact on the Company's financial statements. The timing and measurement of the Company's revenues are not expected to change materially under IFRS 15 because of the nature of the Company's operations and the types of revenues it earns.

(iii) IFRS 16 Leases (effective for annual periods beginning on or after 1 January 2019)

IFRS 16 supersedes IAS 17 Leases and related interpretations. The Standard eliminates the current classification of rent agreements into operating and finance lease for lessees and instead requires companies to bring the agreements that classify as a lease on-balance sheet under a single model.

Under IFRS 16, a contract is, or contains, a lease if it conveys the right to control the use of an identified asset for a period of time in exchange for consideration. For such contracts, the new model requires a lessee to recognise a right-of-use asset and a lease liability. The right-of-use asset is depreciated and the liability accrues interest. This will result in a front-loaded pattern of expense for most leases, even when the lessee pays constant annual rentals.

The Company has not yet prepared an analysis of the expected quantitative impact of the new standard, however, the Company management does not expect that the new standard, when initially applied, will have a material impact on the Company's financial statements. While the Company is party to contractual arrangements that would be in the scope of IFRS 16, their impact on the Company's financial statements is expected to be not material.

(iv) Amendments to IFRS 4: Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (effective for annual periods beginning on or after 1 January 2021)

(v) Amendments to IFRS 2: Classification and Measurement of Share-based Payment Transactions (effective for annual periods beginning on or after 1 January 2018, not yet adopted by the EU)

(vi) Amendments to IAS 40 Transfers of Investment Property (effective for annual periods beginning on or after 1 January 2018, not yet adopted by the EU)

(vii) IFRIC 22 Foreign Currency Transactions and Advance Consideration (effective for annual periods beginning on or after 1 January 2018, not yet adopted by the EU)

(viii) IFRIC 23 Uncertainty over Income Tax Treatments (effective for annual periods beginning on or after 1 January 2019, not yet adopted by the EU)

(ix) Amendments to IFRS 9: Prepayment Features with Negative Compensation (effective for annual periods beginning on or after 1 January 2019, not yet adopted by the EU)

(x) Amendments to IAS 28: Long-term Interests in Associates and Joint Ventures (effective for annual periods beginning on or after 1 January 2019, not yet adopted by the EU)

(xi) Amendments to IAS 19: Plan Amendment, Curtailment or Settlement (effective for annual periods beginning on or after 1 January 2019, not yet adopted by the EU)

(xii) Annual Improvements to IFRSs (Amendments to IFRS 1 First-time Adoption of IFRSs and IAS 28 Investments in Associates and Joint Ventures (effective for annual periods beginning on or after 1 January 2018); Amendments to IFRS 3, IFRS 11, IAS 12 and IAS 23 (effective for annual periods beginning on or after 1 January 2019))

The Company does not plan to adopt these standards early. The Company has assessed the potential impact from new standards and does not expect the new standards to have material impact on the financial statements.

(xiii) IFRS 17 Insurance Contracts (effective for annual periods beginning on or after 1 January 2021, not yet adopted by the EU)

IFRS 17 replaces IFRS 4, which was brought in as an interim Standard in 2004. IFRS 4 has given companies dispensation to carry on accounting for insurance contracts using national accounting standards, resulting in a multitude of different approaches.

IFRS 17 solves the comparison problems created by IFRS 4 by requiring all insurance contracts to be accounted for in a consistent manner, benefiting both investors and insurance companies. Insurance obligations will be accounted for using current values, instead of historical cost.

The Company does not plan to adopt this standard early. The Company expects that this new standard, when initially applied, will have a material impact on the financial statements of the Company as the Company concludes insurance contracts, however, the Company management has not yet started the assessment of the quantitive impact.

2.2.3 Reclassification of balances in the financial statements

In addition, certain balances for 2017 have been classified differently from the prior year, due to management's judgment. There is no impact on the financial result from these reclassifications. Prior year corresponding balances have been reclassified, where appropriate, to conform to current year presentation. The most significant reclassification is that claims handling fees are included in Loss adjustment expenses, while in the financial statement for 2016 they were presented as Other technical income.

2.2.4 Changes in accounting policies

In 2017, the Company has changed its accounting policy for a certain type of long-term property insurance contracts regarding the recognition of premiums and commissions for the consecutive years, which were previously recognized in balance sheet. The effect on prior reporting periods has been calculated and the corresponding amounts in the financial statements have been restated. See Note 24 for additional information.

2.3 Insurance contracts, reinsurance

a) Classification of contracts

Contracts under which the Company accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder are classified as insurance contracts. All contracts concluded are classified as non-life insurance contracts.

Non-life insurance contracts generally have a term of one year. Exceptions include short-term travel insurance policies covering one trip, OMTPL policies with terms of 3, 6 and 9 months (as is stated in the Latvian Law on Obligatory Motor Vehicle Third Party Liability Insurance) where the term is shorter than one year. The policy term may exceed one year for construction liability insurance, although the proportion of these policies in the total portfolio is insignificant.

b) Ceded reinsurance

The Company cedes reinsurance in the normal course of business for the purpose of limiting its net loss potential through the diversification of its risks. Assets, liabilities and income and expense arising from ceded reinsurance contracts are presented separately from the related assets, liabilities, income and expense from the related insurance contracts because the reinsurance arrangements do not relieve the Company from its direct obligations to its policyholders.

Reinsurance assets include the recoveries due from reinsurance companies in respect of claims paid and the reinsurance share in the technical insurance reserves.

The reinsurance share of the incurred but not reported claims technical provision for ceded reinsurance contracts is not recognised for ceded reinsurance contracts as the reinsurance asset cannot be reliably measured.

Amounts recoverable from reinsurers are measured on the basis of the reserve for outstanding claims or the settled claims from policies falling within the scope of a reinsurance contract.

Reinsurance commissions include commissions received or receivable from reinsurers based on the reinsurance contracts. Non-life reinsurance commissions are deferred in a manner consistent with the deferral of acquisition costs in non-life insurance.

Unearned reinsurance commissions are included in the statement of financial position under item Accrued expenses and deferred income.

The main obligatory reinsurance contract forms in reinsurance are excess-of-loss treaties. For risks exceeding the limits of obligatory reinsurance treaties or falling outside their scope due to their nature facultative reinsurance is used.

c) Premiums

Written insurance premiums are insurance premiums for policies, which become effective during the year, irrespective of whether the premium has become due or not. Premiums written are decreased by the premiums cancelled and terminated over the accounting year. Premiums are disclosed gross of commission payable to intermediaries.

The earned portion of premiums written is recognised as revenue. Premiums are recognised as earned on pro-rata basis over the term of the related policy coverage. The unearned portion of premiums is recognised as an unearned premium technical reserve. See section h).

Ceded reinsurance premiums are recognised as an expense in accordance with the pattern of reinsurance service received and the portion of reinsurance premiums attributable for future periods are recognised as assets under the reinsurance part of the unearned premium reserve.

d) Incurred claims

Claims incurred include claims attributable to the reporting year and loss adjustment expenses. Claims paid are decreased by the amount received from salvage or subrogation.

As at the end of reporting period, not settled claims are recognised as outstanding claims technical reserve. See section h).

e) Administrative expenses

Administrative expenses are related to the collection of premiums, management of portfolios, processing of bonuses and discounts and incoming and outgoing reinsurance. They include personnel expenses and depreciation to the extent they are not included in acquisition, claims handling or investing expenses.

Administrative expenses that are not directly related to a specific type of insurance are divided by type of insurance proportionally to the amount of gross written premiums, net earned premiums and insured objects.

f) Client acquisition costs

Acquisition costs of insurance contracts arise from the conclusion of insurance contracts and consists of direct costs such as commissions and indirect expenses incurred related to the conclusion of contracts.

g) Deferred client acquisition costs (DAC)

Commissions and other acquisition costs that vary with and are related to securing new contracts and renewing existing contracts are capitalised as assets. All other client acquisition costs are recognised as expenses when incurred. Deferred client acquisition cost assets are attributed to profit or loss over the terms of the policies as premium is earned on pro-rata basis.

h) Insurance contract liabilities

Unearned premium reserve comprises written gross premium related to period from the balance sheet date to the expiry of insurance agreement to cover all claims and expenses in accordance with insurance agreements in force.

Unexpired risk reserve is set aside for unexpired risks arising from general insurance contracts where the expected value of claims and expenses attributable to the unexpired periods of policies in force at the reporting period end date exceeds the unearned premium reserve in relation to such policies after the deduction of any deferred acquisition costs.

On each reporting date, the Company prepares a Liability adequacy test by assessing whether the insurance liabilities recognized during the reporting year for valid policies are adequate by comparing the insurance reserves established to the present value of the estimated future cash flows arising on existing insurance policies.

If the liability adequacy test shows a deficiency in the carrying amount of liabilities, the deficiency is recognised as a loss for the financial year by setting additional unexpired risk reserve. The test is performed on a “whole insurance portfolio” basis and the test is applied to the net amounts of reserves. Refer to Note 39.

Outstanding claims technical reserve is an amount provided at the end of the reporting year in respect of estimated losses incurred but not yet paid. Outstanding claims reserve includes provisions for reported but not settled claims and provision for incurred but not reported claims. The claims reserve is also created for loss adjustment expenses that will be necessary in order to regulate the claims incurred during the reporting and previous years. Estimated future proceeds from salvage and subrogation related to claims incurred in the reporting and prior years have been deducted from claims reserve.

i) Fronting insurance

As a part of regular business operations, the Company insures risks, which it fully cedes to reinsurers, not keeping the insurance risk or taking full risks to ourselves. Assets, liabilities, as well as income and expenses, which arise from the fronting reinsurance agreements, are presented in Statement of Financial Position of Company, as full ceding of the insurance risk does not release the Company from the direct liabilities to the insurance policy holder.

2.4 Interest income and expense

Interest income and expense are recognised in the income statement for all interest bearing instruments on an accrual basis using the effective interest method. Interest income includes coupons earned on fixed income debt securities, interest on bank deposits and other loans and accrued discounts and premiums on discounted instruments.

2.5 Financial instruments

The Company classifies its financial assets in the following categories: loans and receivables, held to maturity, available for sale and at fair value through profit or loss. The Company classifies all its financial liabilities as liabilities measured using amortized cost. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

a) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables are classified as Loans, Term deposits with banks, Insurance and Reinsurance debtors and Other debtors in the statement of financial position. See accounting policy on Receivables from direct insurance operations. Loans and receivables are measured at amortized cost using the effective interest rate method.

b) Financial liabilities

Financial liabilities classified as liabilities measured using amortized cost are measured at amortized cost using the effective interest rate method.

c) Other financial instruments

The Company's investments in securities are classified as financial assets either held to maturity, available for sale or at fair value through profit or loss. The Company's overall investment objective is to maximize its total return (i.e. interest or dividends and changes in fair value) given a low to medium level of risk and within the given restrictions for the whole portfolio. Accordingly, the Company manages and evaluates the investment portfolio performance on a total return basis.

Financial instruments at fair value through profit or loss are financial assets that are upon initial recognition designated by the entity as at fair value through the profit or loss.

Held-to-maturity instruments are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Company 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 instruments are those financial assets that are designated as available-for-sale or are not classified as loans and receivables, held-to-maturity instruments or financial instruments at fair value through profit or loss.

Purchases and sales of financial assets are recognised on the settlement date – the date on which the Company received or delivered the asset. Loans and receivables and held-to-maturity instruments are initially recognised at fair value plus transaction costs. Available-for-sale instruments and financial assets carried at fair value through profit or loss are initially recognised at fair value, and transaction costs are expensed in the income statement. Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership. Available-for-sale instruments and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables and held-to-maturity instruments are carried at amortised cost using the effective interest method.

Gains or losses arising from changes in the fair value of the financial assets at fair value through profit or loss category are recognised in the profit or loss in the period in which they arise.

The fair values of quoted investments are based on current bid prices. The Company does not have investments in unquoted financial assets at fair value through profit or loss, unquoted financial assets classified as held to maturity or unquoted financial assets classified as available for sale.

Dividends are recognised in the income statement as part of Interest and dividend income. Dividends are recognised in the income statement when the Company's right to receive payments is established.

2.6 Receivables from direct insurance operations

When amounts due from policyholders and intermediaries become overdue the policy is cancelled and respective amounts are reversed against premium written. No impairment allowances are made with respect to amounts that have not yet become due and, accordingly, no portion of the premium is taken to income.

2.7 Intangible assets and property and equipment

All property and equipment and intangible assets (including internally developed software) are stated at historical cost less accumulated depreciation and amortisation and impairment. Land is not depreciated. Depreciation and amortisation on other assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful life using the following rates set by the management:

Buildings	2% per year

Notes to the Financial Statements (All amounts in euros)

Office equipment	20% per year
Computer equipment	25% per year
Internally developed software	20% per year
Vehicles	20% per year
Software	25% per year

Depreciation methods, useful lives and residual values are reviewed at each reporting date and adjusted, if necessary.

The carrying amounts of property and equipment and intangible 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 recognized and the asset's carrying amount is written down to its recoverable amount immediately if the asset's carrying amount exceeds its estimated recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. Impairment losses are recognized in profit or loss.

Subsequent expenditure is capitalised only if it is probable that the future economic benefits associated with the expenditure will flow to the Company. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Leasehold improvements are written down on a straight line basis during leasehold period, but not longer than 5 years.

Profit or loss from disposal of property and equipment is calculated as the difference between the book value of the property and equipment and income generated from sale, and charged to the profit and loss statement as incurred.

2.8 Foreign currency revaluation

Foreign currency transactions are translated into euro applying the euro foreign exchange reference rate published by the European Central Bank at the transaction date. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at the reporting date foreign exchange reference rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement of the respective period.

	31.12.2017	**31.12.2016**
1 USD	EUR 1.19930	EUR 1.05410
1 PLN	EUR 4.17700	EUR 4.41030

2.9 Corporate income tax

a) Current tax

Current tax for the reporting year is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the reporting date (15% as at 31 December 2017), and any adjustment to tax payable in respect of previous years.

As of 1 January 2018, the new Law on Corporate Income Tax of the Republic of Latvia comes into effect, setting out a new regime for paying taxes. As of the date, the tax rate will be 20% instead of the current 15%, the taxation period will be one month instead of a year and the taxable base will include:

- distributed profit (dividends calculated, payments equivalent to dividends, conditional dividends) and
- conditionally or theoretically distributed profit (non-operating expenses, doubtful debts, excessive interest payments, loans to related parties, decrease of income or excessive expenses which are incurred by entering into transactions at prices other than those on the market that should be calculated using the methodology determined by the Cabinet of Ministers, benefits bestowed by the non-resident upon its staff or board (council members) regardless of whether the receiving party is a resident or a non-resident, if they relate to the operation of a permanent establishment in Latvia, liquidation quota).

b) Deferred tax

Deferred income tax is provided for, using the liability method, on all temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax calculations are based on the tax rates effective on the balance sheet date expected to be effective in the periods when the Company will realize the deferred tax asset or settle deferred tax liabilities. Under IAS 12 *Income taxes*, whenever there is a difference to tax rates being applied to distributed and undistributed profits, deferred tax assets and liabilities should be recognised by applying the rate applicable to undistributed profits.

According to the new Law on Enterprise Income Tax of the Republic of Latvia adopted on 28 July 2017, and effective as of 1 January 2018, a 20% rate is only applied to distributed profits while a 0% rate is expected to be applied to undistributed profits. Therefore, deferred tax assets and liabilities are recognisable at nil amount. This principle has been applied in the Company's financial statements for the year ended 31 December 2017.

The carrying amounts of deferred tax assets and liabilities were reversed and changes were charged to profit or loss in the reporting period, except when deferred tax had previously been recognised in relation to revaluation reserve. In that case, the reversal of deferred tax was charged to revaluation reserve as disclosed in Note 26 and recognized in other comprehensive income for the reporting period.

2.10 Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks and other short-term highly liquid investments with original maturities of three months or less. Statement of cash flows is prepared using the direct method.

2.11 Accruals for unused employee vacations

The amount of accruals is determined by multiplying average daily salary for the last six months by the amount of accrued vacation days at the end of the year plus related social tax.

2.12 Administration expense by types of insurance

Other expenses and income, which relate to Company administration and are not directly attributable to a particular sales unit of the Company, are divided as follows:

- the earned premium by the type of customer (legal entity or individual) and by the type of insurance is divided by the total earned premiums to calculate the earned premium proportion;
- total indirect costs are multiplied by the earned premium proportion, which is attributable to the corresponding type of customer and type of insurance.

2.13 Employee benefits

Short-term employee benefits, including salaries and social security contributions, bonuses and vacation benefits, are included in Administrative expenses on accrual basis. The Company calculates annual bonuses for personnel based on previous year financial results and achievement of personal goals. The accruals for personnel bonuses represent the amount accrued as at the year end.

The Company pays social security contributions to the State Social Security Fund (the Fund) on behalf of its employees in accordance with local legal requirements. The Company is required to pay fixed contributions into the Fund and will have no legal or constructive obligations to pay further contributions relating to employee service in the current and prior period. The social security contributions are recognised as an expense on an accrual basis and are included within staff costs.

2.14 Share capital and dividend distribution.

Ordinary shares are classified as equity.

Dividend distribution to the Company's shareholders is recognised as a liability in the financial statements in the period in which the dividends are approved by the Company's shareholders.

2.15 Impairment

a) Financial assets

At each reporting date the Company assesses whether there is objective evidence that financial assets not carried at fair value 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 are impaired can include default or delinquency by a borrower, restructuring of a loan or receivable by the Company on terms that the Group would not otherwise consider, indications that a borrower 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 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.

The Company considers evidence of impairment for loans and receivables at both a specific asset and collective level. All term deposits with credit institutions are assessed for specific impairment.

All individually significant receivables are assessed for specific impairment. All individually significant receivables found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and receivables that are not individually significant are collectively assessed for impairment incurred.

Refer to policy on Receivables from direct insurance operations.

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 receivables. 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.

b) Non-financial assets

The carrying amounts of the Company'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.

Impairment losses recognized 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 recognized.

3. USE OF JUDGEMENTS AND ESTIMATES

Management makes judgments, estimates and assumptions that are applied in the process of preparation of financial statements affect reported amounts of assets and liabilities, income and expenses. Although these estimates are based on management's best knowledge of current events and actions, the actual results ultimately may differ from those estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to the accounting estimates are recognised in the period, in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

The estimation of the ultimate liability arising from claims made under insurance contracts is the Company's most critical accounting estimate.

The provisions for reported but not settled claims (RBNS) are based on claims handler estimate for each individual claim. In cases when a claim is reported but the estimate is not prepared yet, the average claim amount in the corresponding business line is used as an initial reserve.

The provision for incurred but not reported claims (IBNR) is calculated using Bornhuetter - Ferguson method, except for specific insurance portfolios as described below. Obligatory Motor TPL insurers receive recourse claims requests from State Social Insurance Agency (SSIA). Those recourses are reported to insurance companies with the delay of one to two years from accident date to claims recourse reporting date. Recourses are requested for benefits and pensions already paid by SSIA. The Company's claims handlers assess the potential for long-term claim payments and establish a reserve for future payments based on their estimate. The reserve for not yet reported recourses is calculated using the expected claim severity and frequency method which was recommended as the best practice by the Latvian Actuarial Association in 2010 and assessed by the Company as the most appropriate to date. Due to insufficient historical data, IBNR provision for guarantees insurance portfolio and for insurance portfolio taken over from PZU Lietuva Latvian branch in 2015 is calculated using the ultimate loss ratio method where the provision is estimated based on the expected loss ratio for each accident period.

Claims handling reserve is calculated on the basis of average amount for one claim settling transaction and total number of claim transactions estimated for future. The average amount for one claim settling transaction is calculated using historical actual claim administration expense data. Due to insufficient historical data, claims handling reserves for guarantees insurance portfolio and for insurance portfolio taken over from PZU Lietuva Latvian branch in 2015 is calculated using the ultimate loss ratio method where the provision is estimated based on the expected loss ratio for each accident period.

Reserves for recoverable amounts from subrogation and salvage are calculated applying triangle method, i.e., subrogation and salvage amounts are arranged by the periods of accidents and transactions of recovered amounts. Reserves for recoverable amounts from subrogation and salvage are calculated only for those lines of business where regular income is received due to claims specifics therefore probability of recovery is evaluated as high.

Other areas where assumptions and estimation uncertainties are involved are impairment, valuation of deferred acquisition costs. Further information about the assumptions made on those areas are included in the following notes:

- Impairment: Note 2.15
- Deferred acquisition costs: Note 39 about liability adequacy tests performed

As indicated in Note 2.5, all financial assets measured at fair value are quoted. In a fair value hierarchy, based on inputs used in the valuation techniques, these fair values as at 31.12.2017 and as at 31.12.2016 are categorised into Level 1: unadjusted quoted prices in active markets for identical assets.

Notes to the Financial Statements (All amounts in euros)

4. NET WRITTEN PREMIUMS

	2017			2016		
	Gross amount	Reinsurers' share	Net amount	Gross amount	Reinsurers' share	Net amount
Personal accident	2 646 884	(30 002)	2 616 882	1 866 857	(11 078)	1 855 779
Health	16 072 157	-	16 072 157	14 097 920	-	14 097 920
Motor own damage	26 015 594	(548 265)	25 467 329	23 012 076	(403 367)	22 608 709
Marine	29 796	(1 928)	27 868	29 934	(1 099)	28 835
Cargo	930 466	(55 538)	874 928	950 302	(68 067)	882 235
Property	19 482 782	(1 054 596)	18 428 186	18 040 588	(885 616)	17 154 972
Credit insurance	47 006	-	47 006	75 767	-	75 767
General TPL	3 734 422	(244 277)	3 490 145	3 461 468	(207 009)	3 254 459
Guarantees	1 665 918	(565 055)	1 100 863	1 162 337	(422 642)	739 695
Financial risks	432 409	(106 140)	326 269	390 760	(137 026)	253 734
Travel accident	2 864 065	(5 353)	2 858 712	2 437 379	(6 790)	2 430 589
Obligatory Motor TPL	15 000 158	(416 832)	14 583 326	10 084 873	(289 641)	9 795 232
	88 921 657	**(3 027 986)**	**85 893 671**	**75 610 261**	**(2 432 335)**	**73 177 926**

Insurance contracts (policies) are mainly issued to clients residing in Latvia.

Premiums earned

	2017			2016		
	Gross premiums earned	Reinsurers' share	Net premiums earned	Gross premiums earned	Reinsurers' share	Net premiums earned
Motor own damage	24 352 189	(454 755)	23 897 434	21 918 466	(314 237)	21 604 229
Property	19 016 226	(972 257)	18 043 969	17 507 325	(867 567)	16 639 758
Health	15 098 484	-	15 098 484	13 236 464	-	13 236 464
Obligatory Motor TPL	12 502 282	(404 629)	12 097 653	9 823 234	(282 801)	9 540 433
Other	11 162 450	(865 841)	10 296 609	9 412 422	(803 319)	8 609 103
TOTAL	**82 131 631**	**(2 697 482)**	**79 434 149**	**71 897 911**	**(2 267 924)**	**69 629 987**

5. UNEARNED PREMIUM RESERVES

a) Movement in unearned premium reserves

	Gross amount	Reinsurers' share	Net amount
Balance at 31 December 2015	**32 479 125**	**(651 435)**	**31 827 690**
Written premiums	75 610 261	(2 432 335)	73 177 926
Earned premiums	(71 897 911)	2 267 924	(69 629 987)
Total change for the year	3 712 350	(164 411)	3 547 939
Balance at 31 December 2016	**36 191 475**	**(815 846)**	**35 375 629**
Written premiums	88 921 657	(3 027 986)	85 893 671
Earned premiums	(82 131 631)	2 697 482	(79 434 149)
Total change for the year	6 790 026	(330 504)	6 459 522
Balance at 31 December 2017	**42 981 501**	**(1 146 350)**	**41 835 151**

Notes to the Financial Statements (All amounts in euros)

b) Changes in unearned premium reserves and distribution by type of insurance for the year 2017:

	Gross amount	Reinsurers' share	Net amount
Personal accident	454 413	-	454 413
Health	973 673	-	973 673
Motor own damage	1 663 405	(93 510)	1 569 895
Marine	(580)	-	(580)
Cargo	17 323	546	17 869
Property	466 556	(82 339)	384 217
Credit insurance	2 020	-	2 020
General TPL	192 842	(1 029)	191 813
Guarantees	512 699	(147 691)	365 008
Financial risks	(5 827)	5 722	(105)
Travel accident	15 626	-	15 626
Obligatory Motor TPL	2 497 876	(12 203)	2 485 673
	6 790 026	**(330 504)**	**6 459 522**

c) Changes in unearned premium reserves and distribution by type of insurance for the year 2016:

	Gross amount	Reinsurers' share	Net amount
Personal accident	310 989	-	310 989
Health	861 456	-	861 456
Motor own damage	1 093 610	(89 130)	1 004 480
Marine	3 909	-	3 909
Cargo	23 881	450	24 331
Property	533 263	(18 049)	515 214
Credit insurance	(8 368)	-	(8 368)
General TPL	174 159	3 412	177 571
Guarantees	235 566	(57 783)	177 783
Financial risks	12 747	3 529	16 276
Travel accident	209 499	-	209 499
Obligatory Motor TPL	261 639	(6 840)	254 799
	3 712 350	**(164 411)**	**3 547 939**

d) Gross unearned premium reserves as at end of year:

	31.12.2017	31.12.2016
Personal accident	1 496 872	1 042 459
Health	6 380 937	5 407 264
Motor own damage	13 745 960	12 082 555
Marine	12 942	13 522
Cargo	286 514	269 191
Property	10 049 276	9 582 720
Credit insurance	24 996	22 976
General TPL	2 047 571	1 854 729
Guarantees	1 762 350	1 249 651
Financial risks	167 815	173 642
Travel accident	515 150	499 524
Obligatory Motor TPL	6 491 118	3 993 242
	42 981 501	**36 191 475**

Notes to the Financial Statements (All amounts in euros)

6. OTHER TECHNICAL INCOME

	2017	2016
Reinsurance commission income (see Note 36)	206 621	209 272
Income from cancellation of policies	87 268	80 678
Income of agreement penalties	3 840	30 057
Commission income from fronting insurance	32 904	15 162
Changes in provisions for overdue debts, net	2 126	-
Other income	26 486	18 877
	359 245	**354 046**

7. CLAIMS PAID

	2017			2016		
	Gross amount	**Reinsurers' share**	**Net amount**	**Gross amount**	**Reinsurers' share**	**Net amount**
Personal accident	(698 858)	-	(698 858)	(531 198)	-	(531 198)
Health	(10 179 110)	-	(10 179 110)	(9 217 325)	-	(9 217 325)
Motor own damage	(16 455 673)	369 646	(16 086 027)	(14 537 612)	198 349	(14 339 263)
Marine	(34 248)	-	(34 248)	(30 044)	-	(30 044)
Cargo	(286 224)	-	(286 224)	(310 153)	-	(310 153)
Property	(8 810 308)	315 751	(8 494 557)	(11 281 911)	2 868 488	(8 413 423)
Credit insurance	(27 376)	-	(27 376)	(16 634)	-	(16 634)
General TPL	(1 422 196)	-	(1 422 196)	(685 216)	-	(685 216)
Guarantees	(192 625)	52 258	(140 367)	(66 323)	19 513	(46 810)
Financial risks	(503 891)	24 769	(479 122)	(58 496)	-	(58 496)
Travel accident	(651 079)	-	(651 079)	(459 853)	-	(459 853)
Obligatory Motor TPL	(7 667 594)	489 874	(7 177 720)	(7 275 634)	117 451	(7 158 183)
	(46 929 182)	**1 252 298**	**(45 676 884)**	**(44 470 399)**	**3 203 801**	**(41 266 598)**

8. OUTSTANDING CLAIMS RESERVES

a) Movement in outstanding claims reserves:

	2017			2016		
	Gross amount	**Reinsurers' share**	**Net amount**	**Gross amount**	**Reinsurers' share**	**Net amount**
At beginning of year						
Notified claims	15 916 507	(2 963 393)	12 953 114	18 018 901	(5 214 172)	12 804 729
Incurred, but not reported	6 542 241	-	6 542 241	5 588 692	-	5 588 692
Total at beginning of year	**22 458 748**	**(2 963 393)**	**19 495 355**	**23 607 593**	**(5 214 172)**	**18 393 421**
Cash paid for claims notified in prior years	(8 090 435)	692 947	(7 397 488)	(9 527 220)	2 944 935	(6 582 285)
Changes in liabilities arising from current and prior year claims	11 993 620	(2 167 333)	9 826 287	8 378 375	(694 156)	7 684 219
Total change in year	3 903 185	(1 474 386)	2 428 799	(1 148 845)	2 250 779	1 101 934
Total at end of year	**26 361 933**	**(4 437 779)**	**21 924 154**	**22 458 748**	**(2 963 393)**	**19 495 355**
Notified claims	19 189 424	(4 437 779)	14 751 645	15 916 507	(2 963 393)	12 953 114
Incurred, but not reported	7 172 509	-	7 172 509	6 542 241	-	6 542 241
Total at end of year	**26 361 933**	**(4 437 779)**	**21 924 154**	**22 458 748**	**(2 963 393)**	**19 495 355**

Notes to the Financial Statements (All amounts in euros)

b) Change in outstanding claims reserves and distribution by type of insurance for the year 2017:

	Gross amount	Reinsurers' share	Net amount
Personal accident	175 008	(100 000)	75 008
Health	225 151	-	225 151
Motor own damage	381 081	(28 988)	352 093
Marine	(10 715)	-	(10 715)
Cargo	(240 293)	-	(240 293)
Property	1 319 257	(1 012 056)	307 201
Credit insurance	4 825	-	4 825
General TPL	(966 457)	(10 000)	(976 457)
Guarantees	292 762	(75 938)	216 824
Financial risks	944 941	(745 522)	199 419
Travel accident	34 677	-	34 677
Obligatory Motor TPL	1 742 948	498 118	2 241 066
	3 903 185	**(1 474 386)**	**2 428 799**

c) Change in outstanding claims reserves and distribution by type of insurance for the year 2016:

	Gross amount	Reinsurers' share	Net amount
Personal accident	27 961	-	27 961
Health	94 374	-	94 374
Motor own damage	465 004	(72 451)	392 553
Marine	12 918	-	12 918
Cargo	578 025	-	578 025
Property	(2 459 884)	2 402 129	(57 755)
Credit insurance	2 884	-	2 884
General TPL	226 134	-	226 134
Guarantees	242 088	8 430	250 518
Financial risks	964	-	964
Travel accident	18 294	-	18 294
Obligatory Motor TPL	(357 607)	(87 329)	(444 936)
	(1 148 845)	**2 250 779**	**1 101 934**

d) Gross outstanding claims reserves as at end of year:

	31.12.2017	31.12.2016
Personal accident	335 407	160 399
Health	1 194 343	969 192
Motor own damage	3 256 604	2 875 523
Marine	5 159	15 874
Cargo	599 733	840 026
Property	5 659 604	4 340 347
Credit insurance	10 609	5 784
General TPL	1 656 443	2 622 900
Guarantees	835 682	542 920
Financial risks	979 958	35 017
Travel accident	173 822	139 145
Obligatory Motor TPL	11 654 569	9 911 621
	26 361 933	**22 458 748**

Notes to the Financial Statements (All amounts in euros)

9. CLIENT ACQUISITION COSTS

	2017	2016
Commissions to brokers and other intermediaries	(7 851 956)	(6 666 745)
Commissions and other agent related expense	(5 385 103)	(4 982 184)
Compulsory state social security contributions related to agents' remuneration	(1 079 072)	(1 002 597)
Change in deferred client acquisition costs	1 148 931	259 265
Other acquisition expenses	(8 090)	(235)
	(13 175 290)	**(12 392 496)**

Sales costs included in the deferred acquisition costs (DAC) calculation amounting to EUR 4 732 714 (2016: EUR 4 012 432) are represented under Administrative expenses. Refer to Note 10.

Deferred client acquisition costs

As at 31 December 2015	**7 811 763**
Deferred client acquisition costs	16 664 193
Amortisation of deferred acquisition cost	(16 404 928)
As at 31 December 2016	**8 071 028**
Deferred client acquisition costs	19 056 935
Amortisation of deferred acquisition cost	(17 908 004)
As at 31 December 2017	**9 219 959**

10. ADMINISTRATIVE EXPENSES

	2017	2016
Wages and salaries:		
- salaries to staff	(5 375 355)	(4 711 699)
- state compulsory social insurance contributions	(1 174 567)	(1 031 479)
Depreciation and amortization costs	(1 126 649)	(1 291 127)
Advertisement and public relations	(922 915)	(1 119 101)
Information technology and communication expense	(967 318)	(785 885)
Premises utility, maintenance and repair expense	(570 888)	(513 205)
Payments to Motor Insurers Bureau (OMTPL mandatory deductions)	(711 576)	(414 153)
Rent of premises	(299 182)	(272 578)
Payments to Financial and Capital Market Commission	(233 284)	(191 673)
Professional services	(102 566)	(140 393)
Office expenses	(109 050)	(105 786)
Transport	(76 604)	(62 583)
Administration expenses related to Loss adjustment expenses *	423 690	469 224
Other administrative costs	(845 657)	(803 832)
	(12 091 921)	**(10 974 270)**

* – reclassified to and included in Loss adjustment expenses.

In accordance with the requirements of the legislation of the Republic of Latvia payments to Finance and Capital Market Commission have to be made in amount of 0.20% from gross premiums collected in Obligatory Motor Third Party Liability (OMTPL) insurance and in amount of 0.283% from gross premiums collected in other types of insurance. Payments to Foundation of Insured Interests Protection amount to 1.000% of premiums collected from individuals in voluntary types of insurance. In 2017, in accordance with applicable legislation, no payments have been made as the total assets of Foundation of Insured Interests Protection exceeds EUR 11 million.

According to the law "On Obligatory Motor Third Party Liability Insurance" and related regulations of the Cabinet of Ministers of the Republic of Latvia, the Company has to make the following mandatory deductions from Obligatory Motor Third Party Liability insurance gross premiums:

- OMTPL Guarantees Foundation fixed sum for certain type of vehicle; payments were resumed starting from October 2016.
- Road Traffic Accidents Foundation 2% from signed insurance premium during the accounting period.

Notes to the Financial Statements (All amounts in euros)

- Motor Insurers` Bureau of Latvia – a variable sum of EUR 0.50 (2016: EUR 0.50) per contract and a fixed sum of EUR 33 936 per year (2016: EUR 28 080) or EUR 2 828 per month (2015: EUR 2 340).

In 2017, OMTPL mandatory deductions amounted to EUR 711 576 (2016: EUR 414 153).

At the end of year 2017, the Company employed 304 employees (2016: 308) and 267 agents (2016: 278).

Administrative expenses include client acquisition costs amounting to EUR 4 732 714 (2016: EUR 4 012 432) that were included in the calculation of deferred acquisition costs. Such administrative expenses include fixed and variable costs that are related with acquiring new clients and signing policies. Please refer to Note 9.
The remuneration paid to the commercial company of sworn auditors KPMG Baltics SIA for the audit of the financial statements is included in the administrative expenses, and for 2017 amounts to the following: audit of annual financial statements EUR 36 300 (2016: 36 905).

Distribution of administrative expense by type of insurance, based on management allocation, is as follows:

	2017	2016
Personal accident	(448 309)	(349 899)
Health	(2 023 495)	(1 786 381)
Motor own damage	(3 160 764)	(3 114 551)
Marine	(3 697)	(3 572)
Cargo	(135 105)	(107 067)
Property	(2 687 381)	(2 625 461)
Credit insurance	(7 666)	(12 564)
General TPL	(460 400)	(452 219)
Guarantees	(111 279)	(84 450)
Financial risks	(37 218)	(28 360)
Travel accident	(513 478)	(451 489)
Obligatory Motor TPL	(2 503 130)	(1 958 257)
	(12 091 921)	**(10 974 270)**

11. OTHER TECHNICAL EXPENSES

	2017	2016
Changes in provisions for overdue debts, net	-	7 484
Other expenses	466	12 018
	466	**19 502**

12. INTEREST INCOME

	2017	2016
From financial investments at fair value through profit or loss:		
Government bonds	256 235	465 131
Corporate bonds	31 188	31 494
Investment funds	5 388	12 668
From held to maturity financial investments:		
Government bonds	494 961	554 997
Corporate bonds	131 693	85 321
From available for sale financial investments		
Government bonds	683 374	141 759
Corporate bonds	11 804	286
Investment funds	73 678	108
	1 688 321	**1 291 764**

Notes to the Financial Statements (All amounts in euros)

13. NET PROFIT / (LOSS) ON FINANCIAL ASSETS

	2017	2016
Government bonds	(987 418)	(646 407)
Corporate bonds	(87 020)	(62 122)
Investment funds	53 292	261 221
	(1 021 146)	**(447 308)**

	2017	2016
Realised gains / (losses):		
Government bonds	(18 715)	(56 193)
Corporate bonds	(7 479)	-
Investment funds	-	182 712
Unrealised gains / (losses):		
Government bonds	(968 703)	(590 214)
Corporate bonds	(79 541)	(62 122)
Investment funds	53 292	78 509
	(1 021 146)	**(447 308)**

14. OTHER FINANCE INCOME

	2017	2016
Interest on cash and cash equivalents	302	210
	302	**210**

15. OTHER FINANCE EXPENSES

	2017	2016
Accrued interest and amortisation for subordinated loan	(121 560)	(129 303)
Losses from foreign currency fluctuations, net	(11 770)	(1 238)
	(133 330)	**(130 541)**

16. OTHER INCOME

	2017	2016
Income from rent	21 487	21 034
Other income	18 044	2 256
Income from recalculation of social security contributions and VAT	21 056	4 980
	60 587	**28 270**

17. OTHER EXPENSES

	2017	2016
Released receivables from prior years	(75)	(2 690)
Expenses from recalculation of PIT	-	(979)
Other expenses	(14 087)	-
	(14 162)	**(3 669)**

18. CORPORATE INCOME TAX EXPENSES

	2017	2016
Corporate income tax for the reporting year	(619 806)	-
Changes in deferred income tax balances (see Note 26)	(284 850)	(705 943)
Total income tax expense	**(904 656)**	**(705 943)**

Notes to the Financial Statements (All amounts in euros)

Corporate income tax is different from the theoretically calculated amount of tax to be paid if the Company's profit was taxed at the statutory rate:

	2017	2016
Profit before tax	**6 830 216**	**4 730 961**
Theoretically calculated tax at a tax rate of 15%	1 024 532	709 644
Effect of non-deductible expenses and non-taxable income, net	40 455	(3 701)
Effect of tax incentives	(154 951)	-
Effect of changes in legislation – change in the tax rate applicable to undistributed profits (refer to Note 2.9)	(5 380)	-
Total tax	**904 656**	**705 943**

Effective corporate income tax rate in 2017 is 13.24 % (2016: 14.92%).

19. INTANGIBLE ASSETS

	Software	Intangible assets development costs	Total
As at 31 December 2015			
Historical cost	10 835 406	50 710	10 886 116
Accumulated amortization	(8 842 491)	-	(8 842 491)
Net book amount	**1 992 915**	**50 710**	**2 043 625**
In 2016			
Additions arising from internal development	161 593	555 854	717 447
Additions arising from external development	177 403	-	177 403
Reclassified	574 631	(574 631)	-
Written-off	(164 160)	-	(164 160)
Amortization for intangible assets written off	164 138	-	164 138
Amortization charge	(970 853)	-	(970 853)
Closing net book amount	**1 935 667**	**31 933**	**1 967 600**
As at 31 December 2016			
Historical cost	11 584 873	31 933	11 616 806
Accumulated amortization	(9 649 206)	-	(9 649 206)
Net book amount	**1 935 667**	**31 933**	**1 967 600**
In 2017			
Additions arising from internal development	167 189	581 418	748 607
Additions arising from external development	100 458	-	100 458
Reclassified	397 661	(397 661)	-
Written-off	(43 433)	-	(43 433)
Amortization for intangible assets written off	43 433	-	43 433
Amortization charge	(794 963)	-	(794 963)
Closing net book amount	**1 806 012**	**215 690**	**2 021 702**
As at 31 December 2017			
Historical cost	12 250 181	215 690	12 465 871
Accumulated amortization	(10 444 169)	-	(10 444 169)
Net book amount	**1 806 012**	**215 690**	**2 021 702**

Notes to the Financial Statements (All amounts in euros)

20. PROPERTY AND EQUIPMENT

	Land and buildings	Leasehold improve-ments	Transport vehicles	Computers	Office equipment	Total
As at 31 December 2015						
Cost	5 999 396	180 595	62 094	1 660 791	687 817	8 590 693
Accumulated depreciation	(1 616 212)	(71 835)	(52 635)	(1 231 364)	(594 542)	(3 566 588)
Accumulated impairment	(1 997 825)	-	-	-	-	(1 997 825)
Net book amount	**2 385 359**	**108 760**	**9 459**	**429 427**	**93 275**	**3 026 280**
In 2016						
Additions	-	-	-	126 858	24 164	151 022
Disposals	-	-	-	(503 414)	(73 395)	(576 809)
Depreciation charge	(107 736)	(33 046)	(6 310)	(143 936)	(40 207)	(331 235)
Depreciation on disposed assets	-	-	-	503 414	72 654	576 068
Closing net book amount	2 277 623	75 714	3 149	412 349	76 491	2 845 326
As at 31 December 2016						
Cost	5 999 396	180 595	62 094	1 284 235	638 586	8 164 906
Accumulated depreciation	(1 723 948)	(104 881)	(58 945)	(871 886)	(562 095)	(3 321 755)
Accumulated impairment	(1 997 825)	-	-	-	-	(1 997 825)
Net book amount	**2 277 623**	**75 714**	**3 149**	**412 349**	**76 491**	**2 845 326**
In 2017						
Additions	73 972	51 301	103 279	41 954	130 416	400 922
Disposals	(337 141)	-	-	(82 650)	(62 260)	(482 051)
Depreciation charge	(90 140)	(33 626)	(12 452)	(160 579)	(45 853)	(342 650)
Depreciation on disposed assets	327 093	-	-	82 650	62 055	471 798
Closing net book amount	2 251 407	93 389	93 976	293 724	160 849	2 893 345
As at 31 December 2017						
Cost	5 736 227	231 896	165 373	1 243 539	706 742	8 083 777
Accumulated depreciation	(1 486 995)	(138 507)	(71 397)	(949 815)	(545 893)	(3 192 607)
Accumulated impairment	(1 997 825)	-	-	-	-	(1 997 825)
Net book amount	**2 251 407**	**93 389**	**93 976**	**293 724**	**160 849**	**2 893 345**

All land and buildings, and other property and equipment are used in the operating activities of the Company.

21. FINANCIAL INVESTMENTS AT FAIR VALUE THROUGH PROFIT OR LOSS

	31.12.2017 Fair value	Cost	31.12.2016 Fair value	Cost
Latvian government debt securities	8 396 022	7 720 186	10 534 919	9 673 208
Irish government debt	-	-	1 551 588	1 618 500
Corporate bonds	522 817	566 171	853 914	866 882
Investment funds	2 088 638	2 000 000	2 035 346	2 000 000
	11 007 477		**14 975 767**	

The split between current and non-current financial investments at fair value through profit or loss is included in Note 40. Financial investments at fair value through profit or loss in total EUR 11.01 million are in Level 1 fair value hierarchy in accordance with IFRS 7 definitions.

Notes to the Financial Statements (All amounts in euros)

22. HELD TO MATURITY FINANCIAL INVESTMENTS

	31.12.2017 Amortized value	Cost	31.12.2017 Fair value	31.12.2016 Amortized value	Cost	31.12.2016 Fair value
Latvian government debt securities	4 011 681	4 165 003	4 000 073	4 089 370	4 165 003	4 006 855
Bulgarian government debt securities	629 846	633 014	691 920	633 140	633 014	655 662
Croatian government debt securities	397 028	396 082	419 363	399 833	396 082	402 911
Hungarian government debt securities	-	-	-	623 391	646 514	614 250
Lithuanian government debt securities	7 157 645	7 355 071	7 174 000	7 273 306	7 355 071	7 175 750
Polish government debt securities	3 230 666	3 302 628	3 294 800	3 291 468	3 302 628	3 292 036
Slovenian government debt securities	623 630	666 284	606 000	645 903	666 284	630 810
Romanian government debt securities	1 426 077	1 511 728	1 461 590	1 465 129	1 511 728	1 503 515
Corporate bonds	4 410 620	4 396 361	4 507 097	4 452 243	4 396 361	4 513 825
	21 887 193		**22 154 843**	**22 873 783**		**22 795 614**

The split between current and non-current held to maturity financial investments is included in Note 40. Held to maturity financial investments in total EUR 21.89 million are in Level 1 fair value hierarchy in accordance with IFRS 7 definitions.

23. AVAILABLE FOR SALE FINANCIAL INVESTMENTS

	31.12.2017 Fair value	Cost	31.12.2016 Fair value	Cost
Bulgaria government debt securities	2 516 048	2 351 370	2 444 079	2 351 370
Croatia government debt securities	2 624 588	2 493 544	2 029 807	2 004 155
Hungary government debt securities	1 970 195	2 005 330	1 620 240	1 577 216
Polish government debt securities	14 961 241	14 634 071	3 680 660	3 558 503
Romania government debt securities	1 506 092	1 514 302	1 103 568	1 117 000
Lithuania government debt securities	6 380 501	6 380 149	-	-
Corporate bonds	1 587 009	1 561 028	1 044 774	1 045 403
Investment funds	2 817 810	2 805 954	2 812 586	2 805 954
	34 363 484		**14 735 714**	

The split between current and non-current available for sale financial investments is included in Note 40. Available for sale financial investments in total EUR 34.36 million are in Level 1 fair value hierarchy in accordance with IFRS 7 definitions.

The movement of revaluation reserve in respect of available for sale financial investments:

As at 31 December 2015	**-**
Net change in fair value	58 281
Deferred tax effect	(8 742)
As at 31 December 2016	**49 539**
Net change in fair value	475 669
Deferred tax effect	(71 351)
Deferred tax reversal	80 093
As at 31 December 2017	**533 950**

Notes to the Financial Statements (All amounts in euros)

24. RECEIVABLES FROM DIRECT INSURANCE OPERATIONS

	31.12.2017	31.12.2016 (restated)
Gross receivables from direct insurance operations	15 559 839	13 131 943
Doubtful debt allowances for receivables from direct insurance operations	(69 247)	(66 098)
	15 490 592	**13 065 845**

* For information on the restatement refer below.

The ageing of receivables from direct insurance operations at the reporting date was as follows:

	Gross 31.12.2017	Impairment 31.12.2017	Gross 31.12.2016	Impairment 31.12.2016
Not past due	15 147 207	-	12 816 192	-
Past due 0-30 days	266 906	-	241 612	-
Past due 31-60 days	76 479	-	8 041	-
More than 60 days	69 247	(69 247)	66 098	(66 098)
	15 559 839	**(69 247)**	**13 131 943**	**(66 098)**

The management believes that the amounts that are past due by more than 30 days are still collectible in full, based on historic payment behaviour and analysis of customer credit risk.
The movement in the allowance for impairment in respect of receivables from direct insurance operations during the year was as follows:

As at 31 December 2015	**58 614**
Additional allowances	8 363
Recovered debts	(879)
As at 31 December 2016	**66 098**
Additional allowances	5 052
Recovered debts	(1 903)
As at 31 December 2017	**69 247**

* In 2017, the Company has changed its accounting policy for a certain type of long-term property insurance contracts regarding the recognition of premiums and commissions for the consecutive years, which were previously recognized in balance sheet. The change in the policy was applied retrospectively with values of receivables due from policyholders, direct insurance creditors, accrued expenses and deferred income restated as at 31 December 2016, which was the first year when the Company started to recognise the above items in the balance sheet. There is no effect on the total comprehensive income for 2016 and shareholders' equity and reserves as at 31 December 2016 from this change in accounting policy.
Based on the Company management's judgement, the change in the accounting policy will provide a more reliable financial information, as, in line with the applicable insurance contracts provisions, the average historical length of this type of property insurance contracts does not exceed one year.

Due to the change in the accounting policy the corresponding amounts in the financial statements have been restated:

	2016 (as reported previously) EUR	Correction EUR	2016 (restated) EUR
Statement of Financial Position as at 31 December 2016			
Assets			
Receivables due from policyholders	12 918 375	(501 801)	12 416 574
Net effect on Assets		**(501 801)**	
Liabilities			
Direct insurance creditors	3 226 655	(208 146)	3 018 509
Accrued expenses and deferred income	2 807 284	(293 655)	2 513 629
Net effect on Liabilities		**(501 801)**	

Notes to the Financial Statements (All amounts in euros)

25. REINSURANCE RECEIVABLES

	31.12.2017	31.12.2016
Gross receivables from reinsurance operations	532 913	217 591
Doubtful debt allowances for receivables from reinsurance operations	-	-
	532 913	**217 591**

26. DEFERRED TAX ASSETS

	2017	2016
Deferred income tax asset as at the beginning of the reporting year	(276 108)	(990 793)
Changes in deferred income tax recognised to profit or loss statement (see Note 18)	284 850	705 943
Changes in deferred income tax recognised to shareholder's equity (see Note 23)	(8 742)	8 742
Deferred income tax asset as at the end of the reporting year	**-**	**(276 108)**

Deferred income tax is calculated from the following temporary differences between the carrying amounts of assets and liabilities and their values for the purpose of the calculations of corporate income tax:

	31.12.2017	31.12.2016
Temporary difference on depreciation of property and equipment	-	387 137
Temporary difference for accrued expenses	-	(269 340)
Tax loss carry-forwards	-	(376 971)
Temporary difference for impairment for overdue debtors	-	(25 676)
Temporary difference for revaluation reserve of available for sale financial investments	-	8 742
Deferred income tax (asset) / liabilities as at the end of the reporting year	**-**	**(276 108)**

In 2017, the Company adjusted its tax calculation for 2016 due to retrospective derecognition of certain previously recognized taxable temporary differences related to accrued expenses in accordance with the management's judgement. This adjustment resulted in a decrease of EUR 81 843 in the temporary differences for accrued expenses and an increase of EUR 81 843 in the tax loss carried forward, both as at 31 December 2016, however it did not have an effect on the net deferred tax asset calculated as at as at 31 December 2016 or the total income tax expense for 2016.

Movement in deferred tax balances

					31 December 2017	
	Net balance 1 January 2017	**Recognized in profit or loss**	**Recognized in OCI**	**Net balance 31 December 2017**	**Deferred tax asset**	**Deferred tax liability**
Property and equipment	387 137	(387 137)	-	-	-	-
Trade and other receivables	(25 676)	25 676	-	-	-	-
Accrued expenses	(269 340)	269 340	-	-	-	-
Tax loss carry-forwards	(376 971)	376 971	-	-	-	-
Available for sale financial investments	8 742	-	(8 742)	-	-	-
Deferred tax (assets) / liabilities before set-off		**284 850**	**(8 742)**		**-**	**-**
Set off of tax					-	-
Net deferred tax (assets) / liabilities					**-**	**-**

	Net balance 1 January 2016	Recognized in profit or loss	Recognized in OCI	Net balance 31 December 2016	31 December 2016 Deferred tax asset	31 December 2016 Deferred tax liability
Property and equipment	395 498	(8 361)	-	387 137	-	387 137
Trade and other receivables	(29 265)	3 589	-	(25 676)	(25 676)	-
Accrued expenses	(313 007)	43 667	-	(269 340)	(269 340)	-
Tax loss carry-forwards	(1 044 019)	667 048	-	(376 971)	(376 971)	-
Available for sale financial investments	-	-	8 742	8 742	-	8 742
Deferred tax (assets) / liabilities before set-off		**705 943**	**8 742**		**(671 987)**	**395 879**
Set off of tax					395 879	(395 879)
Net deferred tax (assets) / liabilities					**(276 108)**	**-**

27. OTHER ACCRUED INCOME AND DEFERRED EXPENSES

	31.12.2017	31.12.2016
Prepayments for software maintenance	240 551	281 960
Prepayments for rent	26 420	30 575
Insurance payments	8 321	3 585
Reinsurance prepayments	57 226	-
Claims prevention expenses	402 015	91 766
Other deferred expenses	12 873	16 636
	747 406	**424 522**

28. OTHER RECEIVABLES

	31.12.2017	31.12.2016
Financial other receivables		
Receivables for salvage transactions	865 189	732 661
Impairment of overdue salvage settlements	(140 951)	(135 764)
Receivables from other insurance companies	138 550	195 072
Receivables from related parties	12 124	12 124
Receivables for claims regulation	7 114	12 114
Receivables from agents	11 207	7 344
Receivables from the Motor Insurers' Bureau of Latvia	11 055	5 585
Receivables from suitable scrap buyers	5 358	5 122
Other receivables	160 979	207 624
Impairment of other overdue receivables	(135 543)	(140 818)
Total Financial other receivables	**935 082**	**901 064**

Other receivables are due within 12 months from the Statement of Financial Position date and carry no interest.

The movement in the allowance for impairment in respect of other receivables during the year was as follows:

As at 31 December 2015	**334 122**
Additional allowances	-
Recovered debts	(57 540)
As at 31 December 2016	**276 582**
Additional allowances	5 187
Recovered debts	(5 275)
As at 31 December 2017	**276 494**

Notes to the Financial Statements (All amounts in euros)

29. CASH AND CASH EQUIVALENTS

	31.12.2017	31.12.2016
Cash in current accounts	4 111 878	8 688 012
	4 111 878	**8 688 012**

30. SHARE CAPITAL AND RESERVES

a) Issued and fully paid share capital

The total authorised number of ordinary shares is 4 728 064 (31.12.2016: 4 728 064). The nominal value of one share as at 31.12.2017 is EUR 1.4 (31.12.2016: EUR 1.4). All issued shares are fully paid. The share capital of the Company as at
31 December 2017 is EUR 6 619 290 (31.12.2016: EUR 6 619 290).

The Company's shares are not listed.

The holders of ordinary shares are entitled to receive dividends as declared and are entitled to one vote per share at meetings of the Company and to participate in Company's residual assets.

b) The largest shareholder

As at 31.12.2017, the largest shareholder of the Company with 4 727 821 or 99.99% shares (31.12.2016: 4 727 821 shares or 99.99%) is POWSZECHNY ZAKŁAD UBEZPIECZEŃ S.A., a joint-stock company.

c) Share premium

During the increase of share capital in the previous years, according to the share issue rules a share premium was set in addition to the nominal value of the shares.

d) Reserve capital and other reserves

The reserves have been created by transferring profit from retained earnings to these reserves during the previous years in accordance with the applicable past Latvian legislation requirements and shareholders' decisions.

These reserves are available to shareholders, and there are no restrictions on those reserves.

31. TAXES AND THE STATE COMPULSORY SOCIAL INSURANCE CONTRIBUTIONS

	31.12.2017	31.12.2016
Corporate income tax	619 806	-
Compulsory state social security contributions and solidarity tax	324 753	298 207
Personal income tax	157 726	151 946
Value added tax	47 185	30 776
Business risk state duty	208	213
Liabilities	**1 149 678**	**481 142**

During the reporting year, the following tax payments were made:

	2017	2016
Compulsory state social security contributions and solidarity tax	3 697 747	3 457 866
Personal income tax	2 153 773	1 986 185
Value added tax	364 005	324 643
Property tax	32 296	32 296
Business risk state duty	2 528	2 499
Tax withheld from payments to non-residents	-	111
	6 250 349	**5 803 600**

Notes to the Financial Statements (All amounts in euros)

32. ACCRUED EXPENSES AND DEFERRED INCOME

	31.12.2017	31.12.2016 (restated*)
Financial accrued expenses		
Accruals for personnel bonuses	1 456 146	1 066 095
Accrued expenses on unused annual vacations	593 823	545 617
Accruals for intermediary commissions	165 101	115 054
Accruals for consulting services	30 311	53 305
Accruals for rent and utilities services	25 077	23 966
Accruals for audit expenses	18 150	18 150
Accruals for transport expenses	11 918	11 772
Accruals for other expenses	577 073	507 263
Total financial accrued expenses	**2 877 599**	**2 341 222**
Non-financial accrued expenses and deferred income		
Unearned reinsurance commission	251 098	171 453
Other deferred income	321	954
Total non-financial accrued expenses and deferred income	**251 419**	**172 407**
	3 129 018	**2 513 629**

* For information on the restatement refer to Note 24.

	Accruals for personnel bonuses	Other accrued expenses and deferred income	Total
As at 31 December 2016	**1 066 095**	**1 447 534**	**2 513 629**
Additions	1 456 146	1 839 501	3 295 647
Used	(948 461)	(1 559 844)	(2 508 305)
Reversed	(117 634)	(54 319)	(171 953)
As at 31 December 2017	**1 456 146**	**1 672 872**	**3 129 018**
Long-term part	**-**	**239 096**	**239 096**
Short-term part	**1 456 146**	**1 433 776**	**2 889 922**

	Accruals for personnel bonuses	Other accrued expenses and deferred income	Total
As at 31 December 2015	**1 019 018**	**1 222 502**	**2 241 520**
Additions	1 018 353	2 007 608	3 025 961
Used	(695 283)	(1 765 141)	(2 460 424)
Reversed	(275 993)	(17 435)	(293 428)
As at 31 December 2016	**1 066 095**	**1 447 534**	**2 513 629**
Long-term part	**-**	**102 211**	**102 211**
Short-term part	**1 066 095**	**1 345 323**	**2 411 418**

Notes to the Financial Statements (All amounts in euros)

33. OTHER CREDITORS

	31.12.2017	31.12.2016
Financial other creditors		
Commission payables	185 059	177 816
Due to personnel	507 444	454 147
Payables to Group entities	48 315	79 456
Other liabilities	71 992	123 225
Total financial other creditors	**812 810**	**834 644**
Non-financial other creditors		
Due to the Motor Insurers' Bureau of Latvia	121 039	80 194
Due to the Financial and Capital Market Commission	62 345	51 272
Total non-financial other creditors	**183 384**	**131 466**
	996 194	**966 110**
Long-term part	**-**	**-**
Short-term part	**996 194**	**966 110**

34. DIVIDENDS PER SHARE

No dividend distribution is planned to be proposed at the Annual Shareholders' Meeting.

In 2017, the following dividends where declared and paid to the Shareholders of the Company: declared EUR 2 033 068 (2016: EUR 0) or EUR 0.43 (2016: EUR 0) per 1 share; paid: EUR 2 032 978 (2016: EUR 0). In accordance with the Latvian legislation, from the declared dividend amount to shareholders-private persons a personal income tax of 10% is withheld, which in 2017 amounted to EUR 10 (2016: EUR 0). The amount of unpaid dividends as at 31 December 2017 amounted to EUR 90 (31.12.2016: EUR 0).

35. MANDATORY PAYMENTS

Types of mandatory payments made during the reporting year:

	2017	2016
Motor Insurers' Bureau of Latvia	670 727	395 766
Financial and Capital Market Commission	222 211	238 490
	892 938	**634 256**

36. RESULT OF CEDED REINSURANCE

	2017	2016
Reinsurers' share in written premiums (see Note 4)	(3 027 986)	(2 432 335)
Reinsurers' share in changes in unearned premium reserves (see Note 5)	330 504	164 411
Reinsurers' share in claims paid (see Note 7)	1 252 298	3 203 801
Reinsurers' share in changes in outstanding claims reserves (see Note 8)	1 474 386	(2 250 779)
Reinsurance commission income (see Note 6)	206 621	209 272
Net result of ceded reinsurance activities:	**235 823**	**(1 105 630)**

37. TRANSACTIONS AND PAYMENTS TO RELATED PARTIES

Related parties represent both legal entities and private individuals related to the Company in accordance with the following rules:

a) A person or a close member of that person's family is related to a Company if that person:
   - i) has control or joint control over the Company;
   - ii) has significant influence over the Company; or
   - iii) is a member of the key management personnel of the Company or of a parent of the Company.

b) An entity is related to a Company if any of the following conditions applies:
   - i) The entity and the Company are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).
   - ii) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).

iii) Both entities are joint ventures of the same third party.
iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity.
v) The entity is a post-employment benefit plan for the benefit of employees of either the Company or an entity related to the Company. If the Company is itself such a plan, the sponsoring employers are also related to the Company.
vi) The entity is controlled, or jointly controlled by a person identified in (a).
vii) A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).
viii) The entity, or any member of a group of which it is a part, provides key management personnel services to the reporting entity or to the parent of the reporting entity.

The parent company of the Company is POWSZECHNY ZAKŁAD UBEZPIECZEŃ S.A. (Poland).

Lietuvos Draudimas AB is a subsidiary of POWSZECHNY ZAKŁAD UBEZPIECZEŃ S.A.

Lietuvos Draudimas AB Estonia branch is a subsidiary of POWSZECHNY ZAKŁAD UBEZPIECZEŃ S.A.

PZU Lietuva Gyuybes Draudimas UAB is a subsidiary of POWSZECHNY ZAKŁAD UBEZPIECZEŃ S.A.

During the reporting year, the following transactions were carried out with related parties:

a) Transactions with related parties

Reinsurance and fronting insurance

	2017	2016
POWSZECHNY ZAKŁAD UBEZPIECZEŃ S.A. (PZU):		
Reinsurance Premiums ceded	(1 867 632)	(1 549 250)
Change in reinsurers' share in unearned premium reserves	187 136	94 324
Reinsurers' share in claims paid	263 169	2 834 683
Change in reinsurers' share in outstanding claims reserves	429 818	(2 417 101)
Reinsurance Commissions	149 293	76 778
	(838 216)	**(960 566)**

	2017	2016
Lietuvos Draudimas AB:		
Fronting insurance premiums	(420 382)	(263 705)
Commissions from insurance policies fronting	22 215	13 723
Fronting insurance claims	163 209	78 152
Change of fronting insurance unearned premium reserves	130 309	(23 491)
Change of fronting insurance deferred client acquisition costs	(10 046)	(3 469)
Change of fronting insurance outstanding claims reserves	1 433 986	23 629
	1 319 291	**(175 161)**

Other transactions

	2017	2016
Lietuvos Draudimas AB:		
Investment portfolio management services	(6 724)	(79 456)
Indemnity costs, claim handling fee and subrogations	(161 871)	(110 077)
Indemnity costs, claim handling fee and subrogations	57 713	37 757
	(110 882)	**(151 776)**

	2017	2016
POWSZECHNY ZAKŁAD UBEZPIECZEŃ S.A. (PZU):		
Accrued interest and amortisation for subordinated loan	(121 560)	(129 303)
Indemnity costs, claim handling fee and subrogations	(144 262)	(96 404)
Indemnity costs, claim handling fee and subrogations	101 632	41 923
	(164 190)	**(183 784)**

	2017	2016
Lietuvos Draudimas AB Estonia branch:		
Indemnity costs, claim handling fee and subrogations	(150)	-
Indemnity costs, claim handling fee and subrogations	6 732	4 589
	6 582	**4 589**

Notes to the Financial Statements (All amounts in euros)

Balances with related parties

There are the following outstanding balances with related parties as at the reporting date:

	31.12.2017	31.12.2016
POWSZECHNY ZAKŁAD UBEZPIECZEŃ S.A. (PZU):		
Subordinated loan	(2 085 828)	(4 173 022)
Reinsurer's share in unearned premium reserves	(537 663)	-
Reinsurance payables	(322 156)	(210 742)
Total payables	**(2 945 647)**	**(4 383 764)**
Other receivables	99 339	82 039
Reinsurer's share in outstanding claims reserves	483 168	53 350
Reinsurer's share in unearned premium reserves	-	350 527
Unearned reinsurance commissions reserves	189 524	122 684
Reinsurance receivables	230 506	16 843
Total receivables	**1 002 537**	**625 443**
	(1 943 110)	**(3 758 321)**
Lietuvos Draudimas AB:		
Other payables	(48 315)	(79 456)
Fronting insurance reinsurer's share in unearned premium reserves	(190 157)	-
Fronting insurance payables	(159 768)	(96 154)
Total payables	**(398 240)**	**(175 610)**
Fronting insurance reinsurer's share in outstanding claims reserves	1 477 838	43 852
Fronting insurance reinsurer's share in unearned premium reserves	-	59 848
Unearned fronting insurance commissions reserves	10 046	-
Fronting insurance receivables	9 711	72 401
Other receivables	22 061	21 505
Total receivables	**1 519 656**	**176 101**
	1 121 416	**491**
Lietuvos Draudimas AB Estonia branch:		
Other receivables	139	-
	139	**-**
PZU Lietuva Gyuybes Draudimas UAB:		
Other assets (prepayments)	4 487	-
	4 487	**-**
Total payables	(3 343 887)	(4 559 374)
Total receivables	2 526 819	823 049
Net payables	**(817 068)**	**(3 736 325)**

The subordinated loan from PZU has been received on 21 May 2015 for an indefinite period of time with the principal amount of EUR 4 100 000 and a variable interest rate of 3 months EURIBOR + a margin determined on an arm's length basis. The loan is subordinated to all other Company's liabilities. The loan is repayable by the Company no earlier than five years after receiving a repayment notice from the lender, however, the Company also has the right to repay the whole or any part of the loan at any time, subject to providing prior notice and obtaining necessary approvals.

After receiving the consent from Financial Capital and Market Commission for the partial repayment of the loan, the Company repaid a part of the loan on 21 December 2017 in the amount of EUR 2 050 000 and accrued interest in the amount of EUR 34 374 that was calculated for this part of the loan for the time period from the previous interest payment on 29 May 2017 till the repayment on 21 December 2017. The repayment conditions for the remaining part of the loan as at 31 December 2017 have not been changed as a result of this partial repayment.

Notes to the Financial Statements (All amounts in euros)

	Note	Subordinated loan
As at 1 January 2017		**4 173 022**
Changes from financing cash flows		
Repayment of borrowings		(2 050 000)
Interest paid		(158 754)
Total changes from financing cash flows		**(2 208 754)**
Liability-related other changes		
Accrued interest and amortisation	15	121 560
Total liability-related other changes		**121 560**
As at 31 December 2017		**2 085 828**

	Note	Subordinated loan
As at 1 January 2016		**4 179 224**
Changes from financing cash flows		
Repayment of borrowings		-
Interest paid		(135 505)
Total changes from financing cash flows		**(135 505)**
Liability-related other changes		
Accrued interest and amortisation	15	129 303
Total liability-related other changes		**129 303**
As at 31 December 2016		**4 173 022**

b) Management remuneration

In 2017, the Company paid remuneration, including compulsory state social security contributions, to the Management Board in the amount of EUR 998 thousand (2016: EUR 902 thousand) and to the Supervisory Board in the amount of EUR 50 thousand (2016: EUR 56 thousand)

38. CONTINGENT LIABILITIES AND COMMITMENTS

a) General claims

In the normal course of business, the Company constantly receives requests for claim payments. Such claims have been reviewed by the Company's management who is of the opinion that no material unprovided losses will be incurred.

b) Litigation

The Company, like other insurers, is subject to litigation in the normal course of its business. As at 31 December 2017 there were 28 (31.12.2016: 32) pending cases of litigation versus the Company for a total of EUR 1 767 thousand (31.12.2016: EUR 2 519 thousand). The management is of the opinion that no material unrecognized losses will be incurred.

c) Capital commitments

The Company does not have any capital commitments as at 31 December 2017.

The Company does not have any non-cancellable operating leases as at 31 December 2017, other than the rent of premises that usually can be terminated at one to six months' notice. Total minimal commitment for rent payments as at 31 December 2017 amounts to EUR 50 thousand (31.12.2016: EUR 42 thousand).

d) Tax contingencies

The local tax authorities have the power to examine the tax position of the Company for the previous 3 years (5 years for transfer pricing). The Company's management believes that the outcome of tax authority's examination would not result in a material impact on the Company's results and operations or its financial position.

39. INSURANCE RISK MANAGEMENT

The Company issues contracts that transfer insurance risk. This section summarises these risks and the way the Company manages them.

The risk under any one insurance contract is the possibility that the insured event occurs and the uncertainty of the amount of the resulting claim. By the very nature of an insurance contract, this risk is random and therefore unpredictable.

For a portfolio of insurance contracts where the theory of probability is applied to pricing and provisioning, the principal risk that the Company faces under its insurance contracts is that the actual claims payments exceed the carrying amount of the insurance liabilities. This could occur because the frequency or severity of claims is greater than estimated. Insurance events are random and the actual number and amount of claims will vary from year to year from the level established using statistical techniques.

Experience shows that the larger the portfolio of similar insurance contracts, the smaller the relative variability about the expected outcome will be. In addition, a more diversified portfolio is less likely to be affected by a change in any subset of the portfolio. The Company has developed its insurance underwriting strategy to diversify the type of insurance risks accepted and within each of these categories to achieve a sufficiently large population of risks to reduce the variability of the expected outcome.

The frequency and severity of claims can be affected by several factors. The most significant are the increasing level of awards for the damage suffered, and the increase in the number of claim cases. Estimated inflation is also a significant factor due to increased increment rate of inflation.

The Company manages these risks through its underwriting strategy, adequate reinsurance arrangements and proactive claims handling.

The underwriting strategy attempts to ensure that the written risks are well diversified in terms of type and amount of risk, industry and geography.

<u>Types of insurance contracts</u>

Motor third party liability insurance

It is a compulsory insurance type, whose policy conditions and indemnification rules are prescribed by the Motor Third Party Liability Insurance Act and other related legislation. Insurance premiums for motor third party liability are determined individually for each customer based on both customer as well as vehicle based risk criteria. In Latvia, a unified criterion for evaluating the road traffic accident history of a particular vehicle owner – the bonus malus system – is also available.

Most of motor third party liability insurance indemnities are made up of indemnities for property damage and lump sum personal injuries mostly medical treatment costs and temporary incapacity for work benefits. However, long-term indemnities may also be possible, such as pensions and permanent incapacity for work benefits which may be paid out over decades.

Accident insurance

The accident insurance is a money compensation for the death, permanent incapacity for work or trauma arising from an accident. Also refund of costs for medical treatment as well as medical expenses, caused by injury. In addition it is possible to get daily allowances for time spend in hospital and having medical treatment. The insurance amounts are set out on the insurance policy and generally they are not more than 36 thousands euros for death or permanent incapacity for work and 9 euros per day for daily allowances. Typical losses are generally small and they are indemnified as lump sums.

Death events rarely occur on the basis of accident insurance contracts.

Travel insurance

The travel insurance indemnifies for the medical treatment costs incurred during a trip if such costs are caused by an illness or an accident started during the trip. It is also possible to insure a baggage, to purchase insurance against trip cancellations, travel interruptions and delays as well as General Third Party Liability (GTPL) or personal accident coverage. The indemnity limit for the medical treatment and repatriation costs of passenger is limited to 142 thousand euros. A larger risk is related to potential natural disasters in holiday areas or transport crashes, where the number of injured is large. The reinsurance program covers indemnities for losses exceeding 100 thousands euros per occurrence.

Typical losses are generally small and they are indemnified as lump sums. The amount of an indemnity depends on the location of the loss occurrence and the number of claims depends on the season.

Casco insurance

The insurance indemnifies for losses which arise from damage to the vehicle, destruction, theft or robbery of it. Several additional insurance covers may also be purchased which are related to insured vehicle. Insurance premiums are determined individually for each customer based on both customer as well as vehicle based risk criteria. Product package can contain several additional insurance covers – road assistance and replacement car, for instance. Value of insured vehicles commonly does not exceed 71 thousands euros. More than two thirds of losses by amount accumulate from the damage to vehicles sustained in road traffic accidents.

Property insurance, business interruption insurance and building risks insurance

Property insurance covers losses arisen because of fire, weather, leakage of liquid or steam, explosion, malicious acts by third parties (robbery, burglary) or collision. There is a possibility for individuals (private persons) to insure their contents (property) and civil third party liability additionally to private property insurance.

Business interruption insurance covers lost business profits and fixed costs incurred, which arise from the realisation of any risk covered by property insurance of a company.

The largest losses arise from fire risks, which in turn give rise to indemnification for business interruptions. The loss is particularly large if the property (buildings and structures with movables in them) insured to a full extent is destroyed and this leads to a business interruption indemnity until the production object is again put in operation.

The most frequently realised risks for private property include leakage of liquid or steam, fire and weather losses (storm, snowing and flood). The largest losses usually are because of fire.

General liability insurance

This insurance provides coverage for bodily injury and property damage caused to a third party by an insured person, due to its activity or inactivity. In respect of property damages only direct loses are covered, but in respect of bodily injuries direct as well as consequential loses are covered, such as unearned income because of temporary or permanent inability and allowances for dependents. Upon the assessment/ selection of liability insurance risks, it is particularly important to take into account the specifics of customer's commercial activity and customer's turnover.

Health

The health insurance product is offered to companies who purchase health insurance for their employees. The risk covers health insurance indemnities like expenses for doctor visits, hospital expenses, medicaments.

Due to the type of a mass product and large number of small indemnifies along with proper management the risk from this product is small.

Concentration by industry

The concentration of insurance risks by industry do not exceed 20% for an industry, therefore the management is of the opinion that the risk concentration is within the acceptable level.

Reinsurance contract assets

The benefits to which the Company is entitled under its reinsurance contracts held are recognised as reinsurance assets.

These assets consist of short-term balances due from reinsurers as well as longer term receivables that are dependent on the expected claims and benefits arising under the related reinsured insurance contracts. Amounts recoverable from or due to reinsurers are measured consistently with the amounts associated with the reinsured insurance contracts and in accordance with the terms of each reinsurance contract. Reinsurance liabilities are primarily premiums payable for reinsurance contracts and are recognised as an expense when due.

The Company assesses its reinsurance assets for impairment on a regular basis. If there is objective evidence that the reinsurance asset is impaired, the Company reduces the carrying amount of the reinsurance asset to its recoverable amount and recognises that impairment loss in the income statement.

Sensitivity to insurance risk

Based on the fact that the Company provides non-life insurance, only the accounting estimates and assumptions for provision for incurred but not reported claims, as disclosed in Note 3, are assessed by the Company to have a material effect on the timing and uncertainty of the insurer's future cash flows.

The Company performs sensitivity testing of IBNR claim's provisions by detailed analysis of the results calculated by using several statistical methods to ensure that the currently used method gives the best estimate of provisions for IBNR recognized.

Sensitivity analysis for claims provisions at 31.12.2017:

	Impact if loss ratio 5 percent points higher than used in IBNR estimates	**Impact if loss ratio 5 percent points lower than used in IBNR estimates**	**Impact if claims handling expenses 5% higher than used in reserve estimates**	**Impact if claims handling expenses 5% lower than used in reserve estimates**
Obligatory Motor TPL	890 480	(835 277)	20 374	(20 374)
Property	11 188	(11 188)	5 869	(5 869)
Motor own damage	9 528	(9 528)	8 852	(8 852)
General TPL	89 067	(63 508)	4 551	(4 551)
Health	88 276	(88 276)	1 500	(1 500)

Concentration by territory

Insurance contracts (policies) are mainly issued to clients residing in Latvia. The most insured risk territorial coverage is in Latvia.

Geographical concentration of financial assets, financial liabilities and claims reserves as at the reporting date (all amounts in thousands of EUR):

Notes to the Financial Statements *(All amounts in euros)*

Year 2017	Latvia	Other OECD countries	Other countries	Total
Financial assets and reinsurers' share of claims reserves				
Financial investments at fair value through profit or loss	8 396	2 611	-	11 007
Held to maturity financial investments	5 021	7 255	9 611	21 887
Available for sale financial investments	-	20 816	13 547	34 363
Insurance and reinsurance debtors	15 491	523	10	16 024
Reinsurers' share in outstanding claims reserves	-	2 960	1 478	4 438
Cash and cash equivalents	4 112	-	-	4 112
Other debtors	762	148	25	935
Total financial assets and reinsurers' share of claims reserves	**33 782**	**34 313**	**24 671**	**92 766**
Financial liabilities and claims reserves				
Gross outstanding claims reserves	(26 362)	-	-	(26 362)
Financial liabilities (short-term part)	(7 726)	(871)	(214)	(8 811)
Financial liabilities (long-term part)	(363)	(2 086)	-	(2 449)
Total financial liabilities and claims reserves	**(34 451)**	**(2 957)**	**(214)**	**(37 622)**
Net position as at 31 December 2017	**(669)**	**31 356**	**24 457**	**55 144**

Year 2016	Latvia	Other OECD countries	Other countries	Total
Financial assets and reinsurers' share of claims reserves				
Financial investments at fair value through profit or loss	10 843	4 133	-	14 976
Available for sale financial investments	5 099	8 004	9 771	22 874
Held to maturity financial investments	-	9 159	5 577	14 736
Insurance and reinsurance debtors	13 065	146	72	13 283
Reinsurers' share in outstanding claims reserves	-	2 919	44	2 963
Cash and cash equivalents	8 688	-	-	8 688
Other debtors	879	-	22	901
Total financial assets and reinsurers' share of claims reserves	**38 574**	**24 361**	**15 486**	**78 421**
Financial liabilities and claims reserves				
Gross outstanding claims reserves	(22 459)	-	-	(22 459)
Financial liabilities (short-term part)	(5 469)	(727)	(224)	(6 420)
Financial liabilities (long-term part)	(274)	(4 173)	-	(4 447)
Total financial liabilities and claims reserves	**(28 202)**	**(4 900)**	**(224)**	**(33 326)**
Net position as at 31 December 2016	**10 372**	**19 461**	**15 262**	**45 095**

<u>Reinsurance coverage</u>

The reinsurance arrangements include excess and catastrophe coverage. The effect of such reinsurance arrangements is that the Company for each insurance risk has following own retention:

Maximum own retention:

	2017	**2016**
Personal accident & Travel medical expense	90 416	93 864
Cargo insurance	350 000	350 000
Hull, CMR Property	350 000	350 000
Property insurance	678 119	703 977
General TPL insurance	339 060	351 989
Bonds and guarantees	452 080	469 318
Obligatory Motor TPL	400 000	400 000

In 2016 and 2017, there is no reinsurance coverage for Motor own damage under excess of loss reinsurance agreements.

Notes to the Financial Statements (All amounts in euros)

Liability adequacy test

At each balance sheet date, liability adequacy tests are performed to ensure the adequacy of the contract liabilities net of related deferred acquisition costs (DAC) assets. In performing these tests, current best estimates of future contractual cash flows are used. Any deficiency is immediately charged to income statement initially by writing off DAC assets and by subsequently establishing a provision for losses arising from liability adequacy tests (the unexpired risk provision).

Liability adequacy tests as at 31.12.2017 and 31.12.2016 did not identify any impairment of DAC assets.

40. FINANCIAL RISK MANAGEMENT

Risk management framework:

The Company's Management Board has the overall responsibility for the establishment and oversight of the Company's risk management framework. The Management Board monitors the Company's risk management policies which are established to identify and analyse and manage the risks faced by the Company. Policies aim 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 market conditions, products offered and emerging best practice.

The operations of the Company and investment management activities in particular expose it to a variety of financial risks, including credit risk, liquidity risks and market risks, which include interest rate risks, currency risks, as well as fair value risks. The Company's management seeks to minimise potential adverse effects of financial risks on the financial performance of the Company by placing limits on the level of exposure that can be taken.

40.1 Credit risk

The Company takes on exposure to credit risk which is the risk that counterparty will be unable to pay amounts in full when due. The Company structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one issuer of securities, debtor, borrower, or group of the above. Such risks are monitored on a revolving basis and subject to an annual or more frequent review. Actual exposures against limits are monitored regularly.

Exposure to credit risk is managed through regular analysis of the ability of issuers and borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate.

a) Maximum credit exposure

	31.12.2017	**31.12.2016**
Latvian government debt securities	12 407 703	14 624 288
Lithuanian government debt securities	13 538 146	7 273 306
Polish government debt securities	18 191 907	6 972 127
Irish government debt securities	-	1 551 588
Romanian government debt securities	2 932 169	2 568 697
Slovenian government debt securities	623 630	645 903
Hungarian government debt securities	1 970 195	2 243 631
Bulgarian government debt securities	3 145 894	3 077 220
Croatian government debt securities	3 021 616	2 429 640
Corporate bonds	6 520 446	6 350 931
Investment funds	4 906 448	4 847 933
Cash and cash equivalents	4 111 878	8 688 012
	71 370 032	**61 273 276**
Reinsurers' share in unearned premium reserves	1 146 350	815 846
Outstanding claims reserve, reinsurers' share	4 437 779	2 963 393
Reinsurance debtors	532 913	217 591
Receivables due from policyholders	14 486 850	12 918 375
Receivables due from intermediaries	1 003 742	649 271
Other receivables	935 082	901 064
	22 542 716	**18 465 540**
Maximum credit exposure, total	**93 912 748**	**79 738 816**

b) Reinsurance risk breakdown by key counterparties

Reinsurer	31.12.2017 Assets related to reinsurance	Rating*	31.12.2016 Assets related to reinsurance	Rating*
Lietuvas Draudimas	1 677 705	**NR**	176 101	**NR**
Powszechny Zakład Ubezpieczeń SA	1 251 336	**A-**	420 720	**A-**
ALD Re Designated Activity Company	662 292	**NR**	543 761	**NR**
Swiss Re Group	613 990	**AA-**	867 438	**AA-**
Munich Re Group	559 031	**AA-**	572 934	**AA-**
Hannover Re	324 828	**AA-**	341 898	**AA-**
GeneralRensurance AG	292 580	**AA+**	294 464	**AA+**
Caisse Centrale de Reassurances	144 485	**AA**	150 046	**AA**
SCOR Global P&C	137 692	**AA-**	189 019	**AA-**
Lloyd`s Syndicate 1225 AES	100 000	**A**	-	**-**
ACE Tempest Re Europe	79 128	**AA-**	79 128	**AA**
Liberty Syndicate, Cologne	79 128	**A**	79 128	**A**
Odyssey America Reinsurance Corporation	61 399	**A-**	86 744	**A-**
Royal & Sun Alliance Insurance PLC	45 475	**A**	55 171	**A**
R + V Versicherung AG	37 740	**AA-**	75 758	**AA-**
Sirius International Insurance Corporation	29 499	**A-**	29 499	**A-**
Atradius Reinsurance Limited	12 197	**A**	18 569	**A**
Lloyd`s Syndicate 2007 NVA	2 101	**A+**	4 745	**A+**
Nationale Borg Reinsurance N.V.	1 791	**A**	2 615	**A-**
Polish Reinsurance Company	1 722	**A-**	2 490	**A-**
Transatlantic Reinsurance Company	1 553	**A+**	3 507	**A+**
Catlin Insurance Company	1 370	**A+**	3 095	**A+**
Reinsurance risk	**6 117 042**		**3 996 830**	

* Used S&P and A.M. Best agency ratings

c) Investment breakdown by ratings as at the reporting date (all amounts in thousands of EUR):

Year 2017	**Rated AAA**	**AA**	**A**	**BB**	**BBB**	**Total**
Government bonds	-	-	26 569	6 168	23 093	55 830
Corporate bonds	-	-	522	1 869	4 130	6 521
Investment funds	-	-	2 787	-	2 120	4 907
Total investment assets	**-**	**-**	**29 878**	**8 037**	**29 343**	**67 258**

Year 2016	**Rated AAA**	**AA**	**A**	**BB**	**BBB**	**Total**
Government bonds	-	-	24 095	7 750	9 541	41 386
Corporate bonds	-	-	546	1 881	3 924	6 351
Investment funds	-	-	1 015	-	3 833	4 848
Total investment assets	**-**	**-**	**25 656**	**9 631**	**17 298**	**52 585**

40.2 Liquidity risk

The Company is exposed to regular calls on its available cash resources from claims settlements. The Management Board sets the minimum level of cash resources, which must be available to meet such claims.

There has been the following distinction of financial assets, financial liabilities and claims reserves by their remaining maturities as at the reporting date (all amounts in thousands of EUR):

Year 2017	**Non-fixed term**	**up to 12 months**	**1 to 5 years**	**Over 5 years**	**Total**
Financial assets and reinsurers' share of claims reserves					
Financial investments at fair value through profit or loss	2 089	2 677	6 241	-	11 007
Held to maturity financial investments	-	624	6 729	14 534	21 887
Available for sale financial investments	2 818	-	18 129	13 416	34 363
Insurance and reinsurance debtors	-	16 024	-	-	16 024
Reinsurers' share in outstanding claims reserves	-	2 807	1 420	211	4 438
Cash and cash equivalents	4 112	-	-	-	4 112
Other debtors	8	780	147	-	935
Total financial assets and reinsurers' share of claims reserves	**9 027**	**22 912**	**32 666**	**28 161**	**92 766**
Financial liabilities and claims reserves					
Gross outstanding claims reserves	-	(16 448)	(6 978)	(2 936)	(26 362)
Financial liabilities	-	(8 811)	(2 393)	(56)	(11 260)
Total financial liabilities and claims reserves	**-**	**(25 259)**	**(9 371)**	**(2 992)**	**(37 622)**
Net position as at 31 December 2017	**9 027**	**(2 347)**	**23 295**	**25 169**	**55 144**

Year 2016	**Non-fixed term**	**up to 12 months**	**1 to 5 years**	**Over 5 years**	**Total**
Financial assets and reinsurers' share of claims reserves					
Financial investments at fair value through profit or loss	2 035	2 238	6 225	4 478	14 976
Held to maturity financial investments	-	623	6 056	16 195	22 874
Available for sale financial investments	2 813	-	3 449	8 474	14 736
Insurance and reinsurance debtors	-	13 283	-	-	13 283
Reinsurers' share in outstanding claims reserves	-	1 624	975	364	2 963
Cash and cash equivalents	8 688	-	-	-	8 688
Other debtors	-	882	19	-	901
Total financial assets and reinsurers' share of claims reserves	**13 536**	**18 650**	**16 724**	**29 511**	**78 421**
Financial liabilities and claims reserves					
Gross outstanding claims reserves	-	(13 707)	(6 251)	(2 501)	(22 459)
Financial liabilities	-	(6 420)	(4 447)	-	(10 867)
Total financial liabilities and claims reserves	**-**	**(20 117)**	**(10 698)**	**(2 501)**	**(33 326)**
Net position as at 31 December 2016	**13 536**	**(1 477)**	**6 026**	**27 010**	**45 095**

40.3 Market risk

The Company takes on exposure to market risks, which include interest rate risks, currency risks, as well as fair value risks. Market risks arise from open positions in interest rate, share price and currency instruments, all of which are exposed to general and specific market movements. The management sets limits on the value of risk that may be accepted, which is monitored regularly.

a) Exposure to interest rate risk

The Company's exposure to interest rate risk is limited as significant part of liabilities are not bearing interest and dominant part of interest bearing financial instruments have fixed interest rates. Maturity dates are materially equal to reassessment dates on all interest bearing assets and liabilities. Weighted average effective interest rates, as applicable, for the interest bearing financial instruments, excluding insurance contracts, were as follows:

	2017	**2016**
Latvian government debt securities	0.30%	0.33%
Irish government debt securities	-	(0.06%)
Bulgarian government debt securities	0.07%	0.27%
Croatian government debt securities	0.14%	0.46%
Hungarian government debt securities	0.00%	0.03%
Lithuanian government debt securities	0.33%	0.24%
Polish government debt securities	0.46%	0.53%
Slovenian government debt securities	0.01%	0.01%
Romanian government debt securities	0.13%	0.17%
Corporate bonds	0.51%	0.63%
Investment funds	2.41%	1.89%

Risk measurement is regularly analysed by applying back tests and comparing revaluation profit / (loss) from positions with the respective potential risk.

Change in investment value and effect on net result due to market interest rate changes has been as follows:

		2017 EUR	**2016 EUR**
Market interest rate and impact on fair value	+0.5 percent point	(1 405 034)	(1 106 462)
	-0.5 percent point	1 250 511	1 022 831

b) Fair value risk

Financial assets and financial liabilities other than those reflected at their fair value (see Note 21 and Note 23) and those classified as held to maturity (see Note 22), are receivables, cash and cash equivalents, payables and subordinated loan.

Insurance, reinsurance and other financial debtors and financial liabilities, other than subordinated loan, have their remaining maturities of less than one year and carry no interest, thus, their fair value is deemed not to materially differ from their carrying amounts.

Cash and cash equivalents are short-term financial instruments that have their remaining maturities of less than one year and that carry no or little interest, thus, their fair value is deemed not to materially differ from their carrying amounts.

The subordinated loan carries interest in line with market circumstances and terms and conditions of the loan, including the increased risk due to subordination (see Note 37). Taking into account the above, and as there are no material transactions costs related to this loan, its fair value is deemed not to materially differ from its carrying amount.

c) Currency risk

The Company is not exposed to significant currency risk as the reinsurance coverage is provided in, and other transactions are, denominated in EUR. Management of the Company seeks to limit currency risk through an investment portfolio created in respective currencies in the amount equal to respective claims reserves and liabilities.

Split of financial assets, financial liabilities and claims reserves by currencies as at the reporting date (all amounts in thousands of EUR):

Year 2017	USD	EUR	GBP	PLN	Other	Total
Financial assets and reinsurers' share of claims reserves						
Financial investments at fair value through profit or loss	-	11 007	-	-	-	11 007
Held to maturity financial investments	-	21 887	-	-	-	21 887
Available for sale financial investments	-	34 363	-	-	-	34 363
Insurance and reinsurance debtors	14	16 010	-	-	-	16 024
Reinsurers' share in outstanding claims reserves	-	4 438	-	-	-	4 438
Cash and cash equivalents	38	4 048	-	26	-	4 112
Other debtors	-	935	-	-	-	935
Total financial assets and reinsurers' share of claims reserves	**52**	**92 688**	**-**	**26**	**-**	**92 766**
Financial liabilities and claims reserves						
Gross outstanding claims reserves	(59)	(25 853)	(52)	(344)	(54)	(26 362)
Financial liabilities	-	(11 260)	-	-	-	(11 260)
Total financial liabilities and claims reserves	**(59)**	**(37 113)**	**(52)**	**(344)**	**(54)**	**(37 622)**
Net position as at 31 December 2017	**(7)**	**55 575**	**(52)**	**(318)**	**(54)**	**55 144**

Year 2016	USD	EUR	GBP	PLN	Other	Total
Financial assets and reinsurers' share of claims reserves						
Financial investments at fair value through profit or loss	-	14 976	-	-	-	14 976
Held to maturity financial investments	-	22 874	-	-	-	22 874
Available for sale financial investments	-	14 736	-	-	-	14 736
Insurance and reinsurance debtors	16	13 267	-	-	-	13 283
Reinsurers' share in outstanding claims reserves	-	2 963	-	-	-	2 963
Cash and cash equivalents	55	8 612	-	8	13	8 688
Other debtors	-	901	-	-	-	901
Total financial assets and reinsurers' share of claims reserves	**71**	**78 329**	**-**	**8**	**13**	**78 421**
Financial liabilities and claims reserves						
Gross outstanding claims reserves	(73)	(22 158)	(119)	(55)	(54)	(22 459)
Financial liabilities	-	(10 867)	-	-	-	(10 867)
Total financial liabilities and claims reserves	**(73)**	**(33 025)**	**(119)**	**(55)**	**(54)**	**(33 326)**
Net position as at 31 December 2016	**(2)**	**45 304**	**(119)**	**(47)**	**(41)**	**45 095**

Changes in the exchange rates do not have a material impact on net position. The largest share of financial assets and liabilities is held in EUR, which is the Company's functional currency starting from 01.01.2014.

41. CAPITAL RISK MANAGEMENT

Starting from 1 January 2016, the Solvency II regime has come into force. According to this, the Company has established a Capital and Dividend Policy that sets the minimum requirements for measurement, monitoring, controlling and reporting of capital position in order for the Management to take timely and necessary actions. The Company is obliged to achieve and continuously maintain a level of solvency appropriate to the risks the Company undertakes as part of its business activities. The Company anticipates the level of SCR (Solvency Capital requirement) coverage with own funds above the required minimum and acceptable in terms of the Company's Risk Appetite. With continuous growth surplus of assets over liabilities, which translates into financial security and stability, the Company expects to continue having the Solvency Capital requirement above the required minimum also in the future.

42. LOSS DEVELOPMENT TABLE

Loss development table illustrates the Company's estimate of ultimate claims outstanding for each accident year (all amounts in thousands of EUR):

	2007 and prior	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**Total**
Net claims provisions at end of accident year and cumulative incurred claims in subsequent years												
At end of accident year	17 583	12 260	10 106	7 349	5 951	6 411	7 787	8 457	11 114*	10 896*	13 565*	
1 year later	15 812	9 757	8 181	5 771	4 683	4 913	6 679	8 357*	9 115*	8 646*		
2 years later	17 890	8 970	7 977	5 511	4 386	4 999	6 798*	8 189*	8 709*			
3 years later	17 396	8 529	7 999	5 263	4 757	4 850	6 560*	7 668*				
4 years later	16 208	8 775	7 971	5 418	4 804	4 745	6 170*					
5 years later	14 894	8 142	8 019	5 452	4 510	4 434						
6 years later	14 555	8 025	7 879	5 132	4 595							
7 years later	14 411	8 087	7 871	5 105								
8 years later	14 273	8 060	7 956									
9 years later	14 221	8 112										
10 years later	14 167											
Net claims paid												
1 year later	11 320	6 414	5 945	3 933	3 546	3 772	4 880	5 888*	6 054*	5 791*	-	
2 years later	952	342	359	77	279	390	238*	440*	614*			
3 years later	275	269	426	67	411	104	208*	330*				
4 years later	118	361	53	962	39	9	262*					
5 years later	79	63	112	71	132	96						
6 years later	(1)	20	137	(26)	5							
7 years later	389	41	450	(22)								
8 years later	110	32	190									
9 years later	62	21										
10 years later	110											
Cumulative net claims paid	**13 414**	**7 563**	**7 672**	**5 062**	**4 412**	**4 371**	**5 588***	**6 658***	**6 668***	**5 791***	**-**	**67 199***
CY (deficiency) / redundancy	**54**	**(52)**	**(85)**	**27**	**(85)**	**311**	**390****	**521****	**406****	**2 250****	**-**	**3 737****

*) Net claims provisions and net claims paid starting from 2015 include insurance liabilities taken over from PZU Lietuva Latvian branch.

**) Current year (deficiency) / redundancy has been calculated taking into account the net claims provisions of PZU Lietuva Latvian branch as at the moment of business transfer.

43. SUBSEQUENT EVENTS

There are no subsequent events since the last day of the reporting year, which would have a significant effect on the financial statements of the Company as at and for the year ended 31 December 2017.

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Independent Auditors' Report

To the shareholders of AAS BALTA

Report on the Audit of the Financial Statements

Our Opinion on the Financial Statements

We have audited the accompanying financial statements of AAS BALTA ("the Company") set out on pages 8 to 49 of the accompanying Annual Report, which comprise:

- the statement of financial position as at 31 December 2017,
- the statement of comprehensive income for the year then ended,
- the statement of changes in equity for the year then ended,
- the statement of cash flows for the year then ended, and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory notes.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of AAS BALTA as at 31 December 2017, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union.

Basis for Opinion

In accordance with the 'Law on Audit Services' of the Republic of Latvia we conducted our audit in accordance with International Standards on Auditing adopted in the Republic of Latvia (ISAs). Our responsibilities under those standards are further described in the *Auditors' Responsibility for the Audit of the Financial Statements* section of our report.

We are independent of the Company in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and independence requirements included in the 'Law on Audit Services' of the Republic of Latvia that are relevant to our audit of the financial statements in the Republic of Latvia. We have also fulfilled our other professional ethics responsibilities and objectivity requirements in accordance with the IESBA Code and the 'Law on Audit Services' of the Republic of Latvia.

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

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. We have determined the matter described below to be the key audit matter to be communicated in our report.

Measurement of claims reserves

The Company's gross outstanding claims reserves as at 31 December 2017 amounted to EUR 26 361 933 (31 December 2016: EUR 22 458 748). The change in gross outstanding claims reserves in 2017 amounted to EUR 3 903 185 (increase) (in 2016: EUR 1 148 845 (decrease)).

Reference to the financial statements: Note 2.3 h) "Insurance contract liabilities" on page 17 and Note 3 on page 21 (accounting policy); Note 8 "Outstanding claims reserves" on pages 24-25 (Notes to the financial statements).

Key audit matter	*Our response*
Gross outstanding claims reserves ("claim reserves") for the Company, as a non-life insurance provider, constitute the most significant element of insurance contract liabilities presented in the liabilities of the Company's statement of financial position. The most significant claims reserves are associated with the obligatory motor third party liability, motor own damage and property insurance portfolios. Management Board uses a range of complex and subjective actuarial methods to determine the best-estimate amounts of those reserves as at the reporting date, whether in respect of reported claims (i.e. RBNS), or those not reported (i.e. IBNR). The complexity of the models applied may give rise to errors as a result of inaccurate and incomplete data inputs or the design or application of the models. Thus, the completeness and accuracy of the data underlying the actuarial projections was our area of audit focus. The estimation of the amounts of claims reserves generally involves a significant degree of Management Board's judgment, mainly in respect of the assumptions about future events and developments. Relatively insignificant changes in those assumptions may have a significant effect on the estimated amounts of claim reserves. The assumptions most subject to estimation uncertainty are those in respect of loss rates, claim frequency, average claim amounts, court settlements, discount rates, changes in the amount of future annuity	Our audit procedures, performed with the assistance of our actuarial and IT specialists, included, among others: • Testing of the design, implementation and operating effectiveness of key controls related to the process of establishing and adjusting outstanding claims reserves, including the relevant management review controls, accounting and actuarial controls, such as reconciliations of key data underlying the actuarial calculations (such as reports on claims paid and incurred, premiums written and earned and number of claims), as well as testing of general controls in the IT environment regarding data extraction and validation. • Assessing for reasonableness the actuarial methodologies and assumptions applied by the Company, including in particular the loss ratios, claim frequency and average size of claims, expected trends in court settlements, allowance for future claims inflation (including for annuities), discount rates, expected payment dates and payment period, by reference to the methodologies and assumptions applied by the Company in prior period and the prevailing industry practice, also considering the applicable legal and regulatory requirements and the requirements of the relevant financial reporting standards. • For all insurance contract portfolios, performing a retrospective analysis of

payments, and the expected payment period.

Due to the above factors, we considered measurement of the non-life insurance outstanding claims reserves to be our key audit matter.

the accuracy and completeness of the Company's gross outstanding claims reserves recognized at the end of prior year, comparing this analysis to the Company's estimates, and seeking Management Board's explanations for any significant differences.

- For all significant insurance contract portfolios, such as, among others, obligatory motor third party liability, motor own damage and property, developing an independent estimate of the gross outstanding claims reserves, comparing our amount to the Company's estimates and seeking Management Board's explanations for any significant differences.

Reporting on Other Information

The Company's management is responsible for the other information. The other information comprises:

- Information on the Company, as set out on page 3 of the accompanying Annual Report,
- the Report of the Supervisory Board and the Management Board, as set out on pages 4 to 6 of the accompanying Annual Report,
- the Statement of the Supervisory Board's and the Management Board's Responsibility, as set out on page 7 of the accompanying Annual Report.

Our opinion on the financial statements does not cover the other information included in the Annual Report, and we do not express any form of assurance conclusion thereon, except as described in the *Other Reporting Responsibilities in Accordance with the Legislation of the Republic of Latvia Related to Other Information* section of our report.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed and in light of the knowledge and understanding of the Company and its environment obtained in the course of our audit, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Other Reporting Responsibilities in Accordance with the Legislation of the Republic of Latvia Related to Other Information

In addition, in accordance with the 'Law on Audit Services' of the Republic of Latvia with respect to the Report of the Supervisory Board and the Management Board, our responsibility is to consider whether the Report of the Supervisory Board and the Management Board is prepared in accordance with the requirements of the Financial and Capital Market Commission of the Republic of Latvia regulations No. 201 – Regulations on the preparation of annual report and consolidated annual report of insurance and reinsurance undertakings and non-European Union insurance affiliates.

Based solely on the work required to be undertaken in the course of our audit, in our opinion:

- the information given in the Report of the Supervisory Board and the Management Board for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Report of the Supervisory Board and the Management Board has been prepared in accordance with the requirements of the Financial and Capital Market Commission of the Republic of Latvia regulations No. 201 – Regulations on the preparation of annual report and consolidated annual report of insurance and reinsurance undertakings and non-European Union insurance affiliates.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation of the financial statements that give a true and fair view in accordance with IFRSs as adopted by the European Union and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditors' Responsibility for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Company's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves a fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence and objectivity, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on Other Legal and Regulatory Requirements

Other Reporting Responsibilities and Confirmations Required by the Legislation of the Republic of Latvia and the European Union when Providing Audit Services to Public Interest Entities

We were appointed by the extraordinary shareholders' meeting on 3 July 2017 to audit the financial statements of AAS BALTA for the year ended 31 December 2017. Our total uninterrupted period of engagement is 5 years, covering the periods ending 31 December 2013 to 31 December 2017.

We confirm that:

- our audit opinion is consistent with the additional report presented to the Audit Committee of the Company;
- as referred to in the paragraph 37.6 of the 'Law on Audit Services' of the Republic of Latvia we have not provided to the Company the prohibited non-audit services (NASs) referred to of European Union Regulation (EU) No 537/2014. We also remained independent of the audited entity in conducting the audit.

For the period to which our statutory audit relates, we have not provided any services to the Company in addition to the audit.

KPMG Baltics SIA
Licence No. 55

Ondrej Fikrle
Partner pp KPMG Baltics SIA
Riga, Latvia
16 March 2018

Inga Lipšāne
Latvian Certified Auditor
Certificate No. 112