AAS BALTA

Annual Report for 2018 prepared in accordance with the International Financial Reporting Standards as adopted by the European Union and Independent Auditors' Report

Contents

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	Chairman of the Supervisory Board (reappointed on 18.01.2018)
Lidia Maria Orzechowska	Deputy of the Chairman of the Supervisory Board (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 till 26.02.2019)
Pawel Karol Zacharkiewicz	Member of the Supervisory Board (reappointed on 18.01.2018)

Management Board

Name, Surname	*Position*
Iain Kennedy	Chairman of the Management Board
Rafal Piotr Rybkowski	Management Board Member (reappointed on 11.10.2018)
Ingus Savickis	Management Board Member
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 the Latvian Insurers Association and Financial and Capital Market Commission, as well as insurance company public quarterly reports in 2018, BALTA (hereinafter – "Company") has been able to maintain its leading position as the largest company in the Latvian non-life and life (Health, Accident products) insurance market in terms of gross premiums written in Latvia. Significant growth of business and the development of operational excellence have resulted in gross written premiums of 104.7 million EUR and total Net result of insurance activities of 7.4 million EUR for 2018. The continuous profitability has also secured the financial stability of the Company – the capital adequacy (Solvency II) ratio at the end of the year is well above the requirements set by Financial and Capital Market Commission of the Republic of Latvia.

According to data from the Latvian Insurers Association, in 2018 BALTA managed to grow faster than the Latvian non-life and life (Health, Accident products) insurance market by 2.5 percentage points. BALTA has increased its gross written premiums by 15.8 million EUR or 18% compared to 2017, which resulted in a market share of 26%. The Company has managed to grow all of its significant insurance portfolios with the majority of them above the market growth rate.

The wide range of insurance products, excellent customer service and well-considered investments in brand promotion activities have enabled BALTA to retain the leading position in the market not only by volume, but also by customer recognition and brand reputation. BALTA is continuously evaluated as the market leader among insurance companies in terms of awareness, TOP choice and consideration, as well as usage of insurance companies. According to the results of an independent survey of insurance companies in Latvia carried out by LETA and SKDS in 2018, BALTA was recognized as the country's most honest insurer for the 16th year. Additionally to that, in 2018, BALTA received "Most Loved Insurance Company" in Latvia award 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 2018 (InCSR) the Company qualified for Gold category – the only insurance company in Latvia receiving such status. According to the results of a survey of „Aon Best Employers" in 2018, BALTA was recognized as one of the Best Employers in Baltics for the fourth time.

Strong performance of the BALTA brand and reputation is also seen in annual brand research. BALTA possesses the strongest image in the market which is mainly due to high awareness and a large customer base. According to the results of brand research, Top of Mind indicator is 34%, while Total awareness is 91%. BALTA is mostly recognized by customers for positive collaboration experience and excellent service, good reputation and acceptable price offers. BALTA's reputation score among those who know the company is evaluated as 8.0 out of 10, while customer service is 8.5 out of 10. BALTA brand is performing above average and is perceived as the best among its competitors.

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 2018

There was a double digit growth for the second year in a row in the insurance market which reached 15% in accordance with the Latvian Insurers Association data in 2018. This growth is supported by the high economic activity as well as the continuing tail effect of motor segment price increase in the second half of 2017. As a result, the biggest contributors towards growth are MTPL, motor own damage as well as property lines. Despite this growth, Latvian insurance sector penetration in the total economy is still among the lowest in the EU.

In accordance with the Financial and Capital Market Commission data, the Latvian insurers' profitability has slightly declined in 2018, but insurers have still achieved a profit with the combined ratio of 97% in Q3 2018. It is the second profitable year in a row, which has ceased the trend of insurance activity losses from 2011 till 2016. Motor Insurers' Bureau of Latvia data shows that also Motor third party liability insurance has finally started to achieve a profit with the combined ratio of 95%.

Risk management

The Company's Risk Management System is determined by the framework of BALTA's Internal Control System and System of Governance. The Company's business strategy has ensured the establishment of an integrated, consistent and effective risk management system, reflecting the Company's size, scope and complexity. The risk management process consists of the 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 at an individual and at an aggregated level. Each identified risk is subject to monitoring and control in accordance with the procedure specified in dedicated risk management policies by risk category. The method is proportionate to the nature, scale and complexity of this risk. Risk management actions are taken by operational units (first line of defence), the key functions (risk management function, actuarial function, compliance function and financial controlling function), Committees (including 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 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 as determined by the Company.

Capital adequacy and solvency are under constant focus of BALTA. At the end of 2018, the capital of BALTA exceeded the capital required according to law and the rules of the Financial and Capital Market Commission. Stress tests are performed by BALTA within the 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 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 2018, BALTA continued to improve the process of gathering and analysing monthly customer feedback, as well as implemented several feedback system improvements, enabling the Company to introduce new customer oriented initiatives and improve customer service. According to BALTA brand research, customers value BALTA as an insurance company that offers easy-to-understand services, has good reputation and whose service prices are rather acceptable. Almost every fifth customer – 18% – states that BALTA is their first choice.

All customer feedback is analysed on an individual level. Particular suggestions received from customers regarding insurance products and customer service are delivered to sales persons and claims department with the aim to improve BALTA customer cooperation. NPS (Net Promoter Score) surveys are automated (claims) or semi-automated (sales) and overall results are showing a slightly increasing trend.

Additionally, BALTA ensures that overall customer communication is carried out at the appropriate time, innovatively and conveniently. Therefore, one of the largest initiatives launched in 2017 and finalized in 2018 is a project regarding the review of Customer facing documentation, including the development of Customer communication guidelines. These guidelines define the general principles for communication with existing and potential customers of BALTA, including communication types, communication channels, frequency and procedure of communication, as well as the coordination of outgoing communication and its contents.

BALTA launched the Claims self-service module, where it is possible for customers to see the status of each claim, claim decision documentation, directly communicate with the claims handler, and see their claims history. According to customer feedback survey comments, regular Claims handling process reviews are necessary for continuous process improvement. Additionally, Travel claims web notification was launched, and in the first few months already 20% of customers are submitting their claims via this option.

Working environment in the Company and professional development of staff

In 2018, similarly to 2017, BALTA focused on raising employee engagement mainly by improving development opportunities as well as physical working environment. Special attention was given to the onboarding process of new employees and development of new managers. A number of training activities have also been carried out for specialist level employees in order to increase sales and customer service skills, business knowledge and collaboration, raise aspirations, increase personal efficiency and encourage personal growth.

Lean methodology training with practical implementation in processes (as a pilot project) has been carried out. We also continued the Mentoring program, provided career consultations and support for employees' development using coaching methodology.

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

Health and work safety area is strictly controlled and taken care of by internal and external experts. BALTA organizes annual health checks for employees, carries out an annual workplace risk assessment, as well as annual work safety training.

The Company's activities regarding cooperation with employees resulted in both internal and external recognition. Internally, Company improved employee engagement by 2 percentage points reaching 81%, resulting in BALTA being recognized as one of the Best Employers in Baltics for the fourth time. In addition, employee turnover was reduced by 2.2 percentage points.

Externally, for the third year in a row Company received the Family Friendly enterprise award from the Ministry of Welfare of the Republic of Latvia. In 2018, BALTA also achieved the Gold category in the "Working Environment" category in the "Sustainability index - InCSR" Award.

Report of the Supervisory Board and the Management Board

Corporate social responsibility

As the leading insurance company in Latvia, BALTA acts as a responsible member of the society, contributing to the welfare of people not only by supporting the development of business and taking care of its employees and customers, but also by initiating projects of corporate social responsibility (CSR) and strengthening relations with the local communities by providing support. BALTA aims to protect the surrounding world and create change, which will help to create a safer, more sustainable future. BALTA social support principles and priority social support fields are defined in the BALTA Sponsorship and community support policy, and for 2018 they were – safety and prevention, culture, education, and active and healthy lifestyle.

Social support activities in 2018 included sponsorships, donations and gifts, volunteer work and strategic project initiatives with the overall goal of promoting positive changes in the local community. Some of the biggest CSR initiatives carried out in 2018 were BALTA annual award “Safest car fleet” – a contest for businesses with the goal of promoting the education of car fleet managers and overall traffic safety; a child safety campaign in collaboration with the Latvian State Police and also a safe driving campaign related to mobile phone use in collaboration with the Road traffic and safety bureau. In addition, BALTA regularly collaborates with education institutions, educating pupils and students about insurance. BALTA CSR initiatives and activities are also communicated daily through the media and social networks.

In addition to the community support activities, attention is paid to deliver a responsible attitude to customers and partners in the insurance sales process. To align with this value, regular trainings are organized for all stakeholders – insurance agents, sales partners and brokers.

BALTA investments in the community, as well as the ethical and honourable attitude towards customers and business partners, are recognized also by independent experts and the society as a whole. In 2018, BALTA took part in strategic management tool “Sustainability index - InCSR,” which gives the business the opportunity to receive evaluation and suggestions of independent experts in five fields: strategy, market relations, environment, human resources and society support and BALTA qualified for Gold category – the only insurance company in Latvia receiving so high evaluation. Furthermore, for several years BALTA has been taking part in 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.

Proposals regarding distribution of the Company’s profit

In accordance with the Company’s Dividend policy, the Supervisory Board and the Management Board of BALTA do not recommend the distribution of dividends in 2019.

Subsequent events

BALTA has received Anna Teresa Mank's notice of resignation from the position of the Supervisory Board Member of BALTA as of 26 February 2019. BALTA Supervisory Board will operate in an incomplete four members composition until the respective decision of the Shareholders’ meeting. The changes have been registered in the Commercial Register of the Republic of Latvia on 8 March 2019.

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.

Roger Hilton Hodgkiss
Chairman of the Supervisory Board

Iain Kennedy
Chairman of the Management Board

15 March 2019

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 2018 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 2018 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 2018.

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
Chairman of the Supervisory Board

Iain Kennedy
Chairman of the Management Board

15 March 2019

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

	Exhibit	2018	2017
Insurance income			
Gross written premiums	4	104 722 214	88 921 657
Reinsurer's share in written premiums	4	(3 361 080)	(3 027 986)
Net written premiums	4	101 361 134	85 893 671
Change in gross unearned premium and unexpired risk reserves	5	(6 583 939)	(6 790 026)
Change in unearned premium reserves, reinsurers' share	5	(180 580)	330 504
Change in unearned premium and unexpired risk reserves	5	(6 764 519)	(6 459 522)
Net premiums earned		**94 596 615**	**79 434 149**
Other technical income	6	431 937	359 245
Total insurance income		**95 028 552**	**79 793 394**
Insurance expenses			
Gross claims paid to policyholders		(52 230 937)	(47 275 961)
Loss adjustment expenses		(4 104 592)	(3 539 626)
Recovered losses		4 256 978	3 886 405
Claims paid	7	(52 078 551)	(46 929 182)
Reinsurer's share in claims paid	7	3 824 769	1 252 298
Net claims paid		(48 253 782)	(45 676 884)
Change in gross outstanding claims reserves	8	(49 107 125)	(3 903 185)
Change in outstanding claims reserves, reinsurers' share	8	38 948 278	1 474 386
Net incurred claims		**(58 412 629)**	**(48 105 683)**
Client acquisition costs	9	(15 393 933)	(13 175 290)
Administrative expenses	10	(13 842 423)	(12 091 921)
Other technical expenses	11	(12 758)	(466)
Total insurance expenses		**(87 661 743)**	**(73 373 360)**
Net result of insurance activities		**7 366 809**	**6 420 034**
Interest income	12	1 876 427	1 688 321
Net profit / (loss) on financial assets	13	(1 180 288)	(1 021 146)
Investment management expenses		(237 312)	(170 390)
Other finance income	14	186	302
Other finance expenses	15	(67 616)	(133 330)
Other income	16	26 179	60 587
Other expenses	17	(6 166)	(14 162)
Profit before tax		**7 778 219**	**6 830 216**
Changes in deferred income tax asset		-	(284 850)
Corporate income tax for the reporting year		-	(619 806)
Profit for the year		**7 778 219**	**5 925 560**
Other comprehensive income			
Items that are or may be reclassified to profit or loss			
Change in revaluation reserve	23, 24	(641 528)	475 669
Deferred tax effect from changes in revaluation reserve	23	-	8 742
		(641 528)	**484 411**
Other comprehensive income for the period, net of tax		**(641 528)**	**484 411**
Total comprehensive income for the reporting year		**7 136 691**	**6 409 971**

All profit is attributable to the shareholders of AAS BALTA.

Notes on pages 13 to 51 are an integral part of these financial statements.

Roger Hilton Hodgkiss
Chairman of the Supervisory Board

Iain Kennedy
Chairman of the Management Board

15 March 2019

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

	Exhibit	31.12.2018	31.12.2017
ASSETS			
Intangible assets	19	**2 274 222**	**2 021 702**
Property and equipment	20	**3 211 250**	**2 893 345**
Financial investments at fair value through profit or loss	21	4 770 691	11 007 477
Held to maturity financial investments	22	-	21 887 193
Available for sale financial investments	23	-	34 363 484
Financial investments at fair value through other comprehensive income	24	83 341 537	-
Total financial investments		**88 112 228**	**67 258 154**
Receivables due from policyholders		16 407 472	14 486 850
Receivables due from intermediaries		1 109 495	1 003 742
Receivables from direct insurance operations	25	17 516 967	15 490 592
Reinsurance receivables	26	996 113	532 913
Other receivables	28	789 922	935 082
Total receivables		**19 303 002**	**16 958 587**
Reinsurers' share in unearned premium reserves	5	965 770	1 146 350
Reinsurers' share in outstanding claims reserves	8	43 386 057	4 437 779
Reinsurers' share of insurance contract liabilities		**44 351 827**	**5 584 129**
Deferred client acquisition costs	9	10 297 622	9 219 959
Other accrued income and deferred expenses	27	876 389	747 406
Accrued income and deferred expenses		**11 174 011**	**9 967 365**
Cash and cash equivalents	29	**6 671 043**	**4 111 878**
TOTAL ASSETS		**175 097 583**	**108 795 160**

Notes on pages 13 to 51 are an integral part of these financial statements.

Roger Hilton Hodgkiss
Chairman of the Supervisory Board

Iain Kennedy
Chairman of the Management Board

15 March 2019

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

	Exhibit	31.12.2018	31.12.2017
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	23, 24	1 341 345	533 950
Retained earnings		20 485 906	13 496 438
TOTAL SHAREHOLDERS' EQUITY AND RESERVES		**34 399 182**	**26 602 319**
LIABILITIES			
Gross unearned premium and unexpired risk reserves	5	49 565 440	42 981 501
Gross outstanding claims reserves	8	75 469 058	26 361 933
Insurance contract liabilities		**125 034 498**	**69 343 434**
Subordinated loan	37	2 085 897	2 085 828
Direct insurance creditors		7 309 123	4 488 477
Reinsurance creditors		867 255	1 000 212
Taxes and the state compulsory social insurance contributions	31	524 771	1 149 678
Accrued expenses and deferred income	32	3 763 863	3 129 018
Other creditors	33	1 112 994	996 194
Total creditors		**15 663 903**	**12 849 407**
TOTAL LIABILITIES		**140 698 401**	**82 192 841**
TOTAL SHAREHOLDERS' EQUITY, RESERVES AND LIABILITIES		**175 097 583**	**108 795 160**

Notes on pages 13 to 51 are an integral part of these financial statements.

Roger Hilton Hodgkiss
Chairman of the Supervisory Board

Iain Kennedy
Chairman of the Management Board

15 March 2019

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 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**
Adjustment on initial application of IFRS 9*	-	-	-	1 448 923	(788 751)	660 172
Total comprehensive income for the year	**-**	**-**	**-**	**(641 528)**	**7 778 219**	**7 136 691**
Profit for the year	-	-	-	-	7 778 219	7 778 219
Other comprehensive income	**-**	**-**	**-**	**(641 528)**	**-**	**(641 528)**
Net change in revaluation reserve	-	-	-	(641 528)	-	(641 528)
Balance at 31 December 2018	**6 619 290**	**1 595 511**	**4 357 130**	**1 341 345**	**20 485 906**	**34 399 182**

* For additional details, refer to Note 2.2.1.

Notes on pages 13 to 51 are an integral part of these financial statements.

Roger Hilton Hodgkiss
Chairman of the Supervisory Board

Iain Kennedy
Chairman of the Management Board

15 March 2019

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

	Exhibit	2018	2017
Cash flows from operating activities			
Premiums received from direct insurance		103 063 766	86 835 247
Claims paid for direct insurance		(51 702 106)	(46 596 409)
Payments received from ceded reinsurance		1 999 432	447 402
Payments made for ceded reinsurance		(2 671 047)	(1 971 682)
Mandatory payments	35	(1 184 650)	(892 938)
Other expenses		(24 966 374)	(23 498 910)
Net cash from operating activities:		**24 539 021**	**14 322 710**
Cash flows from investing activities			
Disposal of investments		3 861 000	4 282 957
Acquisition of investments		(25 789 677)	(19 286 147)
Purchase of property and equipment and intangible assets		(1 750 692)	(1 198 684)
Proceeds from sale of property and equipment and intangible assets		-	35 998
Interest received from debt securities		1 907 863	1 614 019
Other expenses		(142 590)	(99 372)
Net cash used in investing activities:		**(21 914 096)**	**(14 651 229)**
Cash flows from financing activities			
Repayment of subordinated loan		-	(2 050 000)
Interest paid for subordinated loan		(60 906)	(158 754)
Dividends paid		-	(2 032 978)
Net cash used in financing activities:		**(60 906)**	**(4 241 732)**
Result of foreign exchange rate fluctuations on cash and cash equivalents		**(4 854)**	**(5 883)**
Net increase / (decrease) in cash and cash equivalents		**2 559 165**	**(4 576 134)**
Cash and cash equivalents at the beginning of reporting year		4 111 878	8 688 012
Cash and cash equivalents at the end of reporting year	29	**6 671 043**	**4 111 878**

Notes on pages 13 to 51 are an integral part of these financial statements.

Roger Hilton Hodgkiss
Chairman of the Supervisory Board

Iain Kennedy
Chairman of the Management Board

15 March 2019

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 (Note 2.2.1).

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 15 March 2019. The shareholders have the power to reject the financial statements prepared and issued by the 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 financial instruments carried at fair value through other comprehensive income.

2.1.4 Reporting year

The reporting period comprises the 12 months from 1 January 2018 to 31 December 2018.

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 2018.

(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.

The Company, as an insurance provider, was 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 has not applied the exemption from adopting IFRS 9 and has adopted it as of 1 January 2018 together with the other Group companies.

The Company has adopted IFRS 9 with the effective date of 1 January 2018.The Company has used an exemption not to restate comparative information for prior periods with respect to classification and measurement (including impairment) requirements. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adopting of IFRS 9 are recognized in retained earnings and reserves as at 1 January 2018.

If an investment in a debt security had low credit risk at the date of initial application of IFRS 9, then the Company has assumed that the credit risk on the asset had not increased significantly since its initial recognition.

The following table explains the original measurement categories under IAS 39 and the new measurement categories under IFRS 9 for each class of the Company’s financial assets and financial liabilities as at 1 January 2018 (all amounts in thousands EUR).

	Original classification under IAS 39	New classification under IFRS 9	Original carrying amount under IAS 39	New carrying amount under IFRS 9
Financial assets				
Equity securities (investment funds)	Designated as at FVTPL	Mandatorily at FVTPL	2 089	2 089
Debt securities (sovereign and corporate)	Designated as at FVTPL	FVOCI – debt instrument	8 919	8 919
Equity securities (investment funds)	Available for sale	Mandatorily at FVTPL	2 818	2 818
Debt securities (sovereign and corporate)	Available for sale	FVOCI – debt instrument	31 546	31 546
Debt securities (sovereign and corporate)	Held to maturity	FVOCI – debt instrument	21 887	22 547
Insurance and reinsurance debtors	Loans and receivables	Amortised cost	16 024	16 024
Cash and cash equivalents	Loans and receivables	Amortised cost	4 112	4 112
Other debtors	Loans and receivables	Amortised cost	935	935
Financial liabilities				
Financial liabilities	Other financial liabilities	Other financial liabilities	(11 260)	(11 260)

The following table reconciles the carrying amounts of financial assets under IAS 39 to the carrying amounts under IFRS 9 on transition to IFRS 9 on 1 January 2018 (all amounts in thousands EUR).

	IAS 39 carrying amount as at 31 December 2017	Reclassifi-cation	Remeasure-ment	IFRS 9 carrying amount as at 1 January 2018
Amortized cost				
Cash and cash equivalents				
Brought forward: Loans and receivables	4 112			
Carried forward: Amortized cost				4 112
Insurance and reinsurance debtors				
Brought forward: Loans and receivables	16 024			
Carried forward: Amortized cost				16 024
Other debtors				
Brought forward: Loans and receivables	935			
Carried forward: Amortized cost				935
Debt securities				
Brought forward: Held to maturity	21 887			
Reclassified to: FVOCI – debt		(21 887)		
Total amortized cost	**42 958**	**(21 887)**		**21 071**
FVTPL				
Debt and equity securities				
Brought forward: FVTPL	11 737			
Reclassified to: FVOCI – debt		(8 919)		
Reclassified from: Available for sale		2 088		
Carried forward: FVTPL				4 906
Total FVTPL	**11 737**	**(6 831)**		**4 906**
FVOCI				
Debt and equity securities				
Brought forward: Available for sale	33 634			
Reclassified to: FVOCI – debt		(31 546)		
Reclassified to: FVTPL		(2 088)		
FVOCI – debt				
Debt securities				
Reclassified from: Held to maturity		21 887		
Remeasurement			660	
Reclassified from: Available for sale		31 546		
Reclassified from: FVTPL		8 919		
Remeasurement			(17)	
Carried forward: FVOCI – debt				62 995
Total FVOCI	**33 634**	**28 718**	**643**	**62 995**

As the Company's receivables are mostly short-term, the Company does not estimate a significant impact from the calculation of expected credit loss allowances for Insurance and reinsurance debtors and Other debtors 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 expected credit loss allowances for investments in debt securities according to IFRS 9.

(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.
The Company has adopted IFRS 15 with the effective date of 1 January 2018. The Company's accounting policy has been updated to reflect the terminology in the new standard, but it has had no effect on financial information reported in the current or comparative periods. Because of the nature of the Company's operations and the types of revenues it earns, the timing and measurement of the Company's revenues have not changed materially under IFRS 15, as insurance contracts are out of scope of IFRS 15. The Company recognizes revenue over time (e.g. rent and reinsurance commission income) or at point in time (e.g. sale of salvage, income from cancellation of policies) as the corresponding performance obligations are fulfilled, and there is no significant judgement involved in determining the transaction price or determining when a performance obligation is fulfilled. Revenues in scope of IFRS 15 are included in Statement of Comprehensive Income captions Other technical income, Other income as well as a part of Recovered losses, e.g. for salvage sales transactions. The Company has assessed that IFRS 15 does not have a material impact on the financial statements, and, thus, it does not provide additional disclosures as required by IFRS 15. There has been no restatements of profit or loss for comparative periods.

The following guidance with effective date of 1 January 2018 did not have any effect on these financial statements:

(iii) Amendments to IFRS 2: Classification and Measurement of Share-based Payment Transactions

(iv) Amendments to IFRS 4: Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts

(v) Amendments to IAS 40 Transfers of Investment Property

(vi) Annual Improvements to IFRSs (Amendments to IFRS 1 and IAS 28)

(vii) IFRIC 22 Foreign Currency Transactions and Advance Consideration

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 2019, and have not been applied in preparing these financial statements.

(i) 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 dual accounting model for lessees and instead requires companies to bring most leases on-balance sheet under a single model, eliminating the distinction between operating and finance leases.

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 new Standard introduces a number of limited scope exceptions for lessees which include:

- leases with a lease term of 12 months or less and containing no purchase options, and
- leases where the underlying asset has a low value ('small-ticket' leases).

Lessor accounting, however, shall remain largely unchanged, and the distinction between operating and finance leases will be retained.

It is expected that the IFRS 16, when initially applied, will have a significant impact on the financial statements, since it will require the Company to recognise in its statement of financial position assets and liabilities relating to operating leases for which the Company acts as a lessee.

The Company will recognise new assets and liabilities for its operating leases of premises. The nature and expenses related to those leases will now change because the Company will recognise a depreciation charge for right-of-use assets and interest expense on the lease liabilities. Previously, the Company recognised operating lease expenses on a straight-line basis over the time of the lease, and recognised assets and liabilities only to the extent that there was a timing difference between the actual lease payments and the expense recognised. Based on the information currently available, the Company estimates that it will recognise additional right-of-use asset and lease liability of EUR 930 thousand as at 1 January 2019. The Company does not expect the adoption of IFRS 16 to significantly impact its ability to comply with the Solvency Capital requirement.

The Company plans to apply IFRS 16 initially on 1 January 2019 using the modified retrospective approach. Therefore, the cumulative effect of adopting IFRS 16 will be recognised as an adjustment to the opening balance of retained earnings at 1 January 2019, with no restatement of comparative information. The Company also plans to apply the practical expedient to grandfather the definition of lease on transition. This means that it will apply IFRS 16 to all contracts entered into before 1 January 2019 and identified as leases in accordance with IAS 17 and IFRIC 4.

(ii) IFRIC 23 Uncertainty over Income Tax Treatments (effective for annual periods beginning on or after 1 January 2019)

(iii) Amendments to IFRS 9: Prepayment Features with Negative Compensation (effective for annual periods beginning on or after 1 January 2019)

(iv) 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)

(v) 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)

(vi) Annual Improvements to IFRSs (Amendments to IFRS 3, IFRS 11, IAS 12 and IAS 23 (effective for annual periods beginning on or after 1 January 2019, not yet adopted by the EU))

(vii) Amendments to IFRS 3 Business Combinations (effective for annual periods beginning on or after 1 January 2020, not yet adopted by the EU)

(viii) Amendments to IAS 1 Presentation of Financial Statements and IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors (effective for annual periods beginning on or after 1 January 2020, not yet adopted by the EU)

(ix) Amendments to IFRS 10 and IAS 28 Sale or contribution of assets between an investor and its associate or joint venture (The European Commission decided to defer the endorsement indefinitely.)

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

(x) 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.

2.3 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 by lines of business 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: measured at amortized cost, at fair value through other comprehensive income (FVOCI) and at fair value through profit or loss (VFTPL). The classification of financial assets under IFRS 9 is generally based on the business model in which a financial asset is managed and its contractual cash flow characteristics. 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) Financial assets measured at amortized cost

Financial assets measured at amortized cost using the effective interest rate method are non-derivative financial assets held within a business model whose objective is to hold assets in order to collect contractual cash flows, and whose contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal outstanding. Financial assets measured at amortized cost are classified as Insurance and Reinsurance receivables, Other receivables and Cash and cash equivalents in the statement of financial position. See accounting policy on Receivables from direct insurance operations and Cash and cash equivalents.

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 at fair value through other comprehensive income 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 increase 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.

Financial instruments at fair value through other comprehensive income are financial assets that are upon initial recognition designated by the entity as at fair value through other comprehensive income.

Purchases and sales of financial assets are recognised on the settlement date – the date on which the Company received or delivered the asset. Financial assets measured at amortized cost and financial assets at fair value through other comprehensive income or are initially recognised at fair value plus transaction costs. Financial assets carried at fair value through profit or loss are initially recognised at fair value, and transaction costs are expensed in the statement of profit or loss. 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. Financial assets at fair value through other comprehensive income and at fair value through profit or loss are subsequently carried at fair value. Financial assets measured at amortized cost are carried at amortised cost using the effective interest method.

Notes to the Financial Statements (All amounts in euros)

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 at fair value through other comprehensive income.

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
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.

	31.12.2018	**31.12.2017**
1 USD	EUR 1.1488	EUR 1.19930
1 PLN	EUR 4.2736	EUR 4.17700

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, 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% (till 31.12.2017: 15%) of the distributed profit (dividends calculated, payments equivalent to dividends, conditional dividends).

The new Law on Corporate Income Tax also provides for the application of 20% tax rate to the taxable based, which consists of 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). In accordance with IAS 12 *Income taxes*, income taxes include only such taxes that are based on the taxable profit, thus, corporate income tax calculated on the taxable base consisting of conditionally or theoretically distributed profit is shown under Other expenses.

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 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 2017, 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 and recognized in other comprehensive income for 2017.

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

The Company on a regular basis assesses the expected credit loss of financial assets not carried at fair value.

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

All individually significant receivables are assessed for specific expected credit loss. All individually significant receivables found not to be specifically impaired are then collectively assessed for expected credit loss. Loans and receivables that are not individually significant are collectively assessed for expected credit loss.

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 31.12.2018 and as at 31.12.2017 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

	2018			2017		
	Gross amount	**Reinsurers' share**	**Net amount**	**Gross amount**	**Reinsurers' share**	**Net amount**
Personal accident	2 647 916	(16 710)	2 631 206	2 646 884	(30 002)	2 616 882
Health	18 315 472	-	18 315 472	16 072 157	-	16 072 157
Motor own damage	29 358 906	(246 892)	29 112 014	26 015 594	(548 265)	25 467 329
Marine	28 613	(1 801)	26 812	29 796	(1 928)	27 868
Cargo	947 735	(46 834)	900 901	930 466	(55 538)	874 928
Property	20 823 229	(1 200 163)	19 623 066	19 482 782	(1 054 596)	18 428 186
Credit insurance	55 975	-	55 975	47 006	-	47 006
General TPL	3 985 560	(291 697)	3 693 863	3 734 422	(244 277)	3 490 145
Guarantees	2 376 600	(824 757)	1 551 843	1 665 918	(565 055)	1 100 863
Financial risks	342 185	(110 647)	231 538	432 409	(106 140)	326 269
Travel accident	3 331 560	(7 345)	3 324 215	2 864 065	(5 353)	2 858 712
Obligatory Motor TPL	22 508 463	(614 234)	21 894 229	15 000 158	(416 832)	14 583 326
	104 722 214	**(3 361 080)**	**101 361 134**	**88 921 657**	**(3 027 986)**	**85 893 671**

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

Premiums earned

	2018			2017		
	Gross premiums earned	**Reinsurers' share**	**Net premiums earned**	**Gross premiums earned**	**Reinsurers' share**	**Net premiums earned**
Motor own damage	28 150 356	(544 737)	27 605 619	24 352 189	(454 755)	23 897 434
Property	19 758 885	(1 268 880)	18 490 005	19 016 226	(972 257)	18 043 969
Health	17 419 575	-	17 419 575	15 098 484	-	15 098 484
Obligatory Motor TPL	19 957 776	(607 889)	19 349 887	12 502 282	(404 629)	12 097 653
Other	12 851 683	(1 120 154)	11 731 529	11 162 450	(865 841)	10 296 609
TOTAL	**98 138 275**	**(3 541 660)**	**94 596 615**	**82 131 631**	**(2 697 482)**	**79 434 149**

5. UNEARNED PREMIUM AND UNEXPIRED RISK RESERVES

a) Movement in unearned premium and unexpired risk reserves

	Gross amount	**Reinsurers' share**	**Net amount**
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**
Written premiums	104 722 214	(3 361 080)	101 361 134
Earned premiums	(98 138 275)	3 541 660	(94 596 615)
Total change for the year	6 583 939	180 580	6 764 519
Balance at 31 December 2018	**49 565 440**	**(965 770)**	**48 599 670**

Notes to the Financial Statements (All amounts in euros)

b) Changes in unearned premium and unexpired risk reserves and distribution by type of insurance for the year 2018:

	Gross amount	Reinsurers' share	Net amount
Personal accident	(42 255)	-	(42 255)
Health	895 896	-	895 896
Motor own damage	1 208 550	297 846	1 506 396
Marine	(280)	-	(280)
Cargo	28 704	1 332	30 036
Property	1 064 344	68 718	1 133 062
Credit insurance	12 554	-	12 554
General TPL	123 973	4 419	128 392
Guarantees	718 348	(191 781)	526 567
Financial risks	(35 771)	6 392	(29 379)
Travel accident	59 190	-	59 190
Obligatory Motor TPL	2 550 686	(6 346)	2 544 340
	6 583 939	**180 580**	**6 764 519**

c) Changes in unearned premium and unexpired risk 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**

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

	31.12.2018	31.12.2017
Personal accident	1 454 617	1 496 872
Health	7 276 833	6 380 937
Motor own damage	14 954 510	13 745 960
Marine	12 662	12 942
Cargo	315 218	286 514
Property	11 113 619	10 049 276
Credit insurance	37 550	24 996
General TPL	2 171 544	2 047 571
Guarantees	2 480 698	1 762 350
Financial risks	132 044	167 815
Travel accident	574 340	515 150
Obligatory Motor TPL	9 041 805	6 491 118
	49 565 440	**42 981 501**

Notes to the Financial Statements (All amounts in euros)

6. OTHER TECHNICAL INCOME

	2018	2017
Reinsurance commission income (see Note 36)	264 867	206 621
Income from cancellation of policies	97 705	87 268
Commission income from fronting insurance	29 447	32 904
Income of agreement penalties	6 324	3 840
Changes in provisions for overdue debts, net	-	2 126
Other income	33 594	26 486
	431 937	**359 245**

7. CLAIMS PAID

	2018			2017		
	Gross amount	Reinsurers' share	Net amount	Gross amount	Reinsurers' share	Net amount
Personal accident	(1 139 758)	4 626	(1 135 132)	(698 858)	-	(698 858)
Health	(11 420 448)	-	(11 420 448)	(10 179 110)	-	(10 179 110)
Motor own damage	(16 947 723)	300 722	(16 647 001)	(16 455 673)	369 646	(16 086 027)
Marine	(1 150)	-	(1 150)	(34 248)	-	(34 248)
Cargo	(118 146	3 033	(115 113)	(286 224)	-	(286 224)
Property	(9 869 247)	1 421 240	(8 448 007)	(8 810 308)	315 751	(8 494 557)
Credit insurance	(57 454)	-	(57 454)	(27 376)	-	(27 376)
General TPL	(600 119)	1 060	(599 059)	(1 422 196)	-	(1 422 196)
Guarantees	(874 967)	255 837	(619 130)	(192 625)	52 258	(140 367)
Financial risks	(1 180 307)	1 027 989	(152 318)	(503 891)	24 769	(479 122)
Travel accident	(765 415)	-	(765 415)	(651 079)	-	(651 079)
Obligatory Motor TPL	(9 103 817)	810 262	(8 293 555)	(7 667 594)	489 874	(7 177 720)
	(52 078 551)	**3 824 769**	**(48 253 782)**	**(46 929 182)**	**1 252 298**	**(45 676 884)**

8. OUTSTANDING CLAIMS RESERVES

a) Movement in outstanding claims reserves:

	2018			2017		
	Gross amount	Reinsurers' share	Net amount	Gross amount	Reinsurers' share	Net amount
At beginning of year						
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 beginning of year	**26 361 933**	**(4 437 779)**	**21 924 154**	**22 458 748**	**(2 963 393)**	**19 495 355**
Cash paid for claims notified in prior years	(9 966 178)	2 435 001	(7 531 177)	(8 090 435)	692 947	(7 397 488)
Changes in liabilities arising from current and prior year claims	59 073 303*	(41 383 279)*	17 690 024	11 993 620	(2 167 333)	9 826 287
Total change in year	49 107 125	(38 948 278)	10 158 847	3 903 185	(1 474 386)	2 428 799
Total at end of year	**75 469 058**	**(43 386 057)**	**32 083 001**	**26 361 933**	**(4 437 779)**	**21 924 154**
Notified claims	62 750 438	(43 386 057)	19 364 381	19 189 424	(4 437 779)	14 751 645
Incurred, but not reported	12 718 620	-	12 718 620	7 172 509	-	7 172 509
Total at end of year	**75 469 058**	**(43 386 057)**	**32 083 001**	**26 361 933**	**(4 437 779)**	**21 924 154**

The change in outstanding claims reserves in 2018, among others, is driven by a property claim incurred and notified in 2018 with gross and reinsurers' share in outstanding claims reserves as at 31 December 2018 amounting to EUR 38 497 000 and EUR 37 787 311, correspondingly.

Notes to the Financial Statements (All amounts in euros)

b) Change in outstanding claims reserves and distribution by type of insurance for the year 2018:

	Gross amount	Reinsurers' share	Net amount
Personal accident	257 265	(18 195)	239 070
Health	273 256	-	273 256
Motor own damage	662 555	(32 074)	630 481
Marine	3 303	-	3 303
Cargo	(221 213)	-	(221 213)
Property	39 046 908	(36 928 415)	2 118 493
Credit insurance	7 855	-	7 855
General TPL	252 892	9 800	262 692
Guarantees	557 173	(104 480)	452 693
Financial risks	(692 756)	529 081	(163 675)
Travel accident	(12 110)	-	(12 110)
Obligatory Motor TPL	8 971 997	(2 403 995)	6 568 002
	49 107 125	**(38 948 278)**	**10 158 847**

c) 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**

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

	31.12.2018	31.12.2017
Personal accident	592 672	335 407
Health	1 467 599	1 194 343
Motor own damage	3 919 159	3 256 604
Marine	8 462	5 159
Cargo	378 520	599 733
Property	44 706 512	5 659 604
Credit insurance	18 464	10 609
General TPL	1 909 335	1 656 443
Guarantees	1 392 855	835 682
Financial risks	287 202	979 958
Travel accident	161 712	173 822
Obligatory Motor TPL	20 626 566	11 654 569
	75 469 058	**26 361 933**

Notes to the Financial Statements (All amounts in euros)

9. CLIENT ACQUISITION COSTS

	2018	2017
Commissions to brokers and other intermediaries	(9 551 138)	(7 851 956)
Commissions and other agent related expense	(5 755 110)	(5 385 103)
Compulsory state social security contributions related to agents' remuneration	(1 149 925)	(1 079 072)
Change in deferred client acquisition costs	1 077 662	1 148 931
Other acquisition expenses	(15 422)	(8 090)
	(15 393 933)	**(13 175 290)**

Deferred client acquisition costs

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**
Deferred client acquisition costs	21 797 679
Amortisation of deferred acquisition cost	(20 720 016)
As at 31 December 2018	**10 297 622**

Client acquisition costs included in the deferred acquisition costs (DAC) calculation amounting to EUR 5 326 084 (2017: EUR 4 732 714) are represented under Administrative expenses. Refer to Note 10.

10. ADMINISTRATIVE EXPENSES

	2018	2017
Wages and salaries:		
- salaries to staff	(6 042 606)	(5 375 355)
- state compulsory social insurance contributions	(1 384 416)	(1 174 567)
Depreciation and amortization costs	(1 171 184)	(1 126 649)
Advertisement and public relations	(1 073 449)	(922 915)
Information technology and communication expense	(1 176 411)	(967 318)
Premises utility, maintenance and repair expense	(569 977)	(570 888)
Payments to Motor Insurers Bureau (OMTPL mandatory deductions)	(979 945)	(711 576)
Rent of premises	(317 498)	(299 182)
Payments to Financial and Capital Market Commission	(273 014)	(233 284)
Professional services	(233 490)	(102 566)
Office expenses	(132 535)	(109 050)
Transport	(77 956)	(76 604)
Administration expenses related to Loss adjustment expenses *	480 744	423 690
Other administrative costs	(890 686)	(845 657)
	(13 842 423)	**(12 091 921)**

* – 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 2018, 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.
- 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 0.48 (2017: EUR 0.50) per contract and a fixed sum of EUR 34 896 per year (2017: EUR 33 936) or EUR 2 908 per month (2017: EUR 2 828).

In 2018, OMTPL mandatory deductions amounted to EUR 979 945 (2017: EUR 711 576).

At the end of year 2018, the Company employed 314 employees (2017: 304) and 255 agents (2017: 267).

Administrative expenses include client acquisition costs amounting to EUR 5 326 084 (2017: EUR 4 732 714) 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 certified auditors KPMG Baltics SIA for the audit of the financial statements is included in the administrative expenses, and for 2018 amounts to the following: audit of annual financial statements, incl. VAT: EUR 36 300 (2017: 36 300).

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

	2018	**2017**
Personal accident	(545 753)	(448 309)
Health	(2 298 755)	(2 023 495)
Motor own damage	(3 326 852)	(3 160 764)
Marine	(3 584)	(3 697)
Cargo	(113 868)	(135 105)
Property	(2 734 622)	(2 687 380)
Credit insurance	(8 757)	(7 666)
General TPL	(513 766)	(460 400)
Guarantees	(168 369)	(111 279)
Financial risks	(33 476)	(37 218)
Travel accident	(618 397)	(513 478)
Obligatory Motor TPL	(3 476 224)	(2 503 130)
	(13 842 423)	**(12 091 921)**

11. OTHER TECHNICAL EXPENSES

	2018	**2017**
Changes in provisions for overdue debts, net	12 616	-
Other expenses	142	466
	12 758	**466**

12. INTEREST INCOME

	2018	**2017**
From financial investments at fair value through profit or loss:		
Government bonds	-	256 235
Corporate bonds	-	31 188
Investment funds	10 587	5 388
From held to maturity financial investments:		
Government bonds	-	494 961
Corporate bonds	-	131 693
From available for sale financial investments		
Government bonds	-	683 374
Corporate bonds	-	11 804
Investment funds	-	73 678
From financial investments at fair value through other comprehensive income		
Government bonds	1 616 145	-
Corporate bonds	198 847	-
Investment funds	50 848	-
	1 876 427	**1 688 321**

Notes to the Financial Statements (All amounts in euros)

13. NET PROFIT / (LOSS) ON FINANCIAL ASSETS

	2018	2017
Government bonds	(974 761)	(987 418)
Corporate bonds	(69 770)	(87 020)
Investment funds	(135 757)	53 292
	(1 180 288)	**(1 021 146)**

	2018	2017
Realised gains / (losses):		
Government bonds	(8 169)	(18 715)
Corporate bonds	(12 125)	(7 479)
Investment funds	(37 104)	-
Unrealised gains / (losses):		
Government bonds	(966 592)	(968 703)
Corporate bonds	(54 949)	(79 541)
Investment funds	(98 654)	53 292
Changes in Expected credit losses	(2 695)	-
	(1 180 288)	**(1 021 146)**

14. OTHER FINANCE INCOME

	2018	2017
Interest on cash and cash equivalents	186	302
	186	**302**

15. OTHER FINANCE EXPENSES

	2018	2017
Accrued interest and amortisation for subordinated loan	(60 975)	(121 560)
Losses from foreign currency fluctuations, net	(6 641)	(11 770)
	(67 616)	**(133 330)**

16. OTHER INCOME

	2018	2017
Other income	12 797	18 044
Income from rent	7 150	21 487
Income from recalculation of social security contributions, PIT and VAT	6 232	21 056
	26 179	**60 587**

17. OTHER EXPENSES

	2018	2017
Other expenses	(5 674)	(14 087)
Expenses from recalculation of PIT and social security contributions	(492)	-
Released receivables from prior years	-	(75)
	(6 166)	**(14 162)**

18. CORPORATE INCOME TAX EXPENSES

	2018	2017
Corporate income tax for the reporting year	-	(619 806)
Changes in deferred income tax balances (see Note 26)	-	(284 850)
Total income tax expense	**-**	**(904 656)**

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:

	2018	2017
Profit before tax	**7 778 219**	**6 830 216**
Theoretically calculated tax at a tax rate of 0% (2017: 15%)	-	1 024 532
Effect of non-deductible expenses and non-taxable income, net	-	40 455
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**

Effective corporate income tax rate in 2018 is 0 % (2017: 13.24%).

19. INTANGIBLE ASSETS

	Software	Intangible assets development costs	Total
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**
In 2018			
Additions arising from internal development	223 144	732 623	955 767
Additions arising from external development	82 803	-	82 803
Reclassified	855 060	(855 060)	-
Written-off	(216 835)	-	(216 835)
Amortization for intangible assets written off	216 835	-	216 835
Amortization charge	(786 049)	-	(786 049)
Closing net book amount	**2 180 970**	**93 253**	**2 274 223**
As at 31 December 2018			
Historical cost	13 194 352	93 253	13 287 605
Accumulated amortization	(11 013 383)	-	(11 013 383)
Net book amount	**2 180 969**	**93 253**	**2 274 222**

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 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**
In 2018						
Additions	(172)	102 328	-	478 020	131 946	712 122
Disposals	179 949	-	-	(277 143)	(95 896)	(193 090)
Depreciation charge	(68 259)	(36 473)	(20 663)	(211 711)	(56 940)	(394 046)
Depreciation on disposed assets	(179 949)	-	-	276 972	95 896	192 919
Closing net book amount	2 182 976	159 244	73 313	559 862	235 855	3 211 250
As at 31 December 2018						
Cost	5 916 004	334 224	165 373	1 444 416	742 792	8 602 809
Accumulated depreciation	(1 735 203)	(174 980)	(92 060)	(884 554)	(506 937)	(3 393 734)
Accumulated impairment	(1 997 825)	-	-	-	-	(1 997 825)
Net book amount	**2 182 976**	**159 244**	**73 313**	**559 862**	**235 855**	**3 211 250**

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

	31.12.2018 Fair value	Cost	31.12.2017 Fair value	Cost
Latvian government debt securities	-	-	8 396 022	7 720 186
Corporate bonds	-	-	522 817	566 171
Investment funds	4 770 691	4 783 849	2 088 638	2 000 000
	4 770 691		**11 007 477**	

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 4.77 million (2017: EUR 11.01 million) are in Level 1 fair value hierarchy in accordance with IFRS 7 definitions.

In line with the Company's initial application of IFRS 9 as of 1 January 2018, a part of the financial investments classified at fair value through profit or loss until 31 December 2017 were reclassified to financial investments at fair value through other comprehensive income. For additional details, refer to Note 2.2.1.

Notes to the Financial Statements (All amounts in euros)

22. HELD TO MATURITY FINANCIAL INVESTMENTS

	31.12.2018 Amortized value	Cost	31.12.2018 Fair value	31.12.2017 Amortized value	Cost	31.12.2017 Fair value
Latvian government debt securities	-	-	-	4 011 681	4 165 003	4 000 073
Bulgarian government debt securities	-	-	-	629 846	633 014	691 920
Croatian government debt securities	-	-	-	397 028	396 082	419 363
Hungarian government debt securities	-	-	-	-	-	-
Lithuanian government debt securities	-	-	-	7 157 645	7 355 071	7 174 000
Polish government debt securities	-	-	-	3 230 666	3 302 628	3 294 800
Slovenian government debt securities	-	-	-	623 630	666 284	606 000
Romanian government debt securities	-	-	-	1 426 077	1 511 728	1 461 590
Corporate bonds	-	-	-	4 410 620	4 396 361	4 507 097
	-		-	**21 887 193**		**22 154 843**

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 as at 31 December 2017 were in Level 1 fair value hierarchy in accordance with IFRS 7 definitions.

In line with the Company's initial application of IFRS 9 as of 1 January 2018, financial investments classified as held to maturity until 31 December 2017 were reclassified to financial investments at fair value through other comprehensive income. For additional details, refer to Note 2.2.1.

23. AVAILABLE FOR SALE FINANCIAL INVESTMENTS

	31.12.2018 Fair value	Cost	31.12.2017 Fair value	Cost
Bulgaria government debt securities	-	-	2 516 048	2 351 370
Croatia government debt securities	-	-	2 624 588	2 493 544
Hungary government debt securities	-	-	1 970 195	2 005 330
Polish government debt securities	-	-	14 961 241	14 634 071
Romania government debt securities	-	-	1 506 092	1 514 302
Lithuania government debt securities	-	-	6 380 501	6 380 149
Corporate bonds	-	-	1 587 009	1 561 028
Investment funds	-	-	2 817 810	2 805 954
	-		**34 363 484**	

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 as at 31 December 2017 were in Level 1 fair value hierarchy in accordance with IFRS 7 definitions.
In line with the Company's initial application of IFRS 9 as of 1 January 2018, financial investments classified as available for sale until 31 December 2017 were reclassified to financial investments at fair value through other comprehensive income. For additional details, refer to Note 2.2.1.

Notes to the Financial Statements (All amounts in euros)

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

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**
Transferred to financial investments at fair value through other comprehensive income	(533 950)
As at 31 December 2018	**-**

In line with the Company's initial application of IFRS 9 as of 1 January 2018, the revaluation reserve was transferred to financial investments at fair value through other comprehensive income.

24. FINANCIAL INVESTMENTS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME

	31.12.2018		**31.12.2017**	
	Fair value	**Cost**	**Fair value**	**Cost**
Lithuania government debt securities	30 002 375	30 345 452	-	
Latvian government debt securities	17 978 040	17 777 686	-	-
Polish government debt securities	17 895 907	17 936 700	-	-
Bulgaria government debt securities	3 154 621	2 984 384	-	
Croatia government debt securities	3 015 595	2 889 626	-	-
Romania government debt securities	2 883 136	3 026 030	-	-
Hungary government debt securities	1 876 442	2 005 330	-	-
Corporate bonds	6 535 421	6 460 289	-	-
	83 341 537		**-**	

The movement of revaluation reserve in respect of financial investments at fair value through other comprehensive income:

As at 31 December 2016	**-**
As at 31 December 2017	**-**
Transferred from available for sale financial investments	533 950
Adjustment on initial application of IFRS 9	1 448 923
Net change in fair value	(641 528)
As at 31 December 2018	**1 341 345**

25. RECEIVABLES FROM DIRECT INSURANCE OPERATIONS

	31.12.2018	**31.12.2017**
Gross receivables from direct insurance operations	17 602 752	15 559 839
Doubtful debt allowances for receivables from direct insurance operations	(85 785)	(69 247)
	17 516 967	**15 490 592**

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

	Gross 31.12.2018	**Allowances 31.12.2018**	**Net 31.12.2018**	**Gross 31.12.2017**	**Allowances 31.12.2017**	**Net 31.12.2017**
Not past due	17 197 218	-	17 197 218	15 147 207	-	15 147 207
Past due 0-30 days	303 754	-	303 754	266 906	-	266 906
Past due 31-60 days	15 995	-	15 995	76 479	-	76 479
More than 60 days	85 785	(85 785)	-	69 247	(69 247)	-
	17 602 752	**(85 785)**	**17 516 967**	**15 559 839**	**(69 247)**	**15 490 592**

Notes to the Financial Statements (All amounts in euros)

The management believes that the amounts that are not past due and past due by no more than 60 days are still collectible in full, based on historic payment behaviour and analysis of customer credit risk, and impairment allowance for expected credit loss is not recognized due to being considered as immaterial.

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 2016	**66 098**
Additional allowances	5 052
Recovered debts	(1 903)
As at 31 December 2017	**69 247**
Additional allowances	19 065
Recovered debts	(2 527)
As at 31 December 2018	**85 785**

26. REINSURANCE RECEIVABLES

	31.12.2018	31.12.2017
Gross receivables from reinsurance operations	996 113	532 913
Doubtful debt allowances for receivables from reinsurance operations	-	-
	996 113	**532 913**

The management believes that receivables from reinsurance operations are collectible in full, based on historic payment behaviour and analysis of reinsurers' credit risk, and impairment allowance for expected credit loss is not recognized due to being considered as immaterial.

27. OTHER ACCRUED INCOME AND DEFERRED EXPENSES

	31.12.2018	31.12.2017
Claims prevention expenses	510 298	402 015
Prepayments for software maintenance	262 874	240 551
Reinsurance prepayments	53 879	57 226
Prepayments for rent	27 602	26 420
Other deferred expenses	17 537	12 873
Insurance payments	4 199	8 321
	876 389	**747 406**

28. OTHER RECEIVABLES

	31.12.2018	31.12.2017
Financial other receivables		
Receivables for subrogation transactions	615 162	865 189
Impairment of overdue subrogation settlements	(139 137)	(140 951)
Receivables from other insurance companies	252 065	138 550
Receivables from related parties	12 124	12 124
Receivables for claims regulation	7 114	7 114
Receivables from agents	5 910	11 207
Receivables from the Motor Insurers' Bureau of Latvia	14 224	11 055
Receivables from suitable scrap buyers	-	5 358
Other receivables	154 081	160 979
Impairment of other overdue receivables	(131 621)	(135 543)
Total Financial other receivables	**789 922**	**935 082**

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

Notes to the Financial Statements (All amounts in euros)

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

As at 31 December 2016	**276 582**
Additional allowances	5 187
Recovered debts	(5 275)
As at 31 December 2017	**276 494**
Additional allowances	-
Recovered debts	(5 736)
As at 31 December 2018	**270 758**

29. CASH AND CASH EQUIVALENTS

	31.12.2018	31.12.2017
Cash in current accounts	6 671 043	4 111 878
	6 671 043	**4 111 878**

The management believes that Cash in current accounts is collectible in full, based on historic payment behaviour and analysis of corresponding credit institutions' credit risk, and impairment allowance for expected credit loss is not recognized due to being considered as immaterial.

30. SHARE CAPITAL AND RESERVES

a) Issued and fully paid share capital

The total authorised number of ordinary shares is 4 728 064 (31.12.2017: 4 728 064). The nominal value of one share as at 31.12.2018 is EUR 1.4 (31.12.2017: EUR 1.4). All issued shares are fully paid. The share capital of the Company as at
31 December 2018 is EUR 6 619 290 (31.12.2017: 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 31.12.2018, the largest shareholder of the Company with 4 727 821 or 99.99% shares (31.12.2017: 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

	31.12.2018	31.12.2017
Corporate income tax	-	619 806
Compulsory state social security contributions and solidarity tax	330 331	324 753
Personal income tax	157 642	157 726
Value added tax	36 591	47 185
Business risk state duty	207	208
Liabilities	**524 771**	**1 149 678**

Notes to the Financial Statements (All amounts in euros)

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

	2018	2017
Compulsory state social security contributions and solidarity tax	4 320 700	3 697 747
Personal income tax	2 285 184	2 153 773
Corporate income tax	619 806	-
Value added tax	520 952	364 005
Property tax	31 846	32 296
Business risk state duty	2 487	2 528
	7 780 975	**6 250 349**

32. ACCRUED EXPENSES AND DEFERRED INCOME

	31.12.2018	31.12.2017
Financial accrued expenses		
Accruals for personnel bonuses	1 849 029	1 456 146
Accrued expenses on unused annual vacations	667 914	593 823
Accruals for intermediary commissions	192 969	165 101
Accruals for consulting services	2 178	30 311
Accruals for rent and utilities services	30 525	25 077
Accruals for audit expenses	18 150	18 150
Accruals for transport expenses	12 803	11 918
Accruals for other expenses	707 748	577 073
Total financial accrued expenses	**3 481 316**	**2 877 599**
Non-financial accrued expenses and deferred income		
Unearned reinsurance commission	282 226	251 098
Other deferred income	321	321
Total non-financial accrued expenses and deferred income	**282 547**	**251 419**
	3 763 863	**3 129 018**

	Accruals for personnel bonuses	Other accrued expenses and deferred income	Total
As at 31 December 2017	**1 456 146**	**1 672 872**	**3 129 018**
Additions	1 664 824	2 384 497	4 049 321
Used	(1 220 413)	(1 983 805)	(3 204 218)
Reversed	(51 528)	(158 730)	(210 258)
As at 31 December 2018	**1 849 029**	**1 914 834**	**3 763 863**
Long-term part	**184 204**	**244 268**	**428 472**
Short-term part	**1 664 825**	**1 670 566**	**3 335 391**

	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**

33. OTHER CREDITORS

	31.12.2018	31.12.2017
Financial other creditors		
Commission payables	192 655	185 059
Due to personnel	558 617	507 444
Payables to Group entities	50 600	48 315
Other liabilities	59 432	71 992
Total financial other creditors	**861 304**	**812 810**
Non-financial other creditors		
Due to the Motor Insurers' Bureau of Latvia	181 826	121 039
Due to the Financial and Capital Market Commission	69 864	62 345
Total non-financial other creditors	**251 690**	**183 384**
	1 112 994	**996 194**
Long-term part	**-**	**-**
Short-term part	**1 112 994**	**966 194**

34. DIVIDENDS PER SHARE

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

35. MANDATORY PAYMENTS

Types of mandatory payments made during the reporting year:

	2018	2017
Motor Insurers' Bureau of Latvia	919 159	670 727
Financial and Capital Market Commission	265 491	222 211
	1 184 650	**892 938**

36. RESULT OF CEDED REINSURANCE

	2018	2017
Reinsurers' share in written premiums (see Note 4)	(3 361 080)	(3 027 986)
Reinsurers' share in changes in unearned premium reserves (see Note 5)	(180 580)	330 504
Reinsurers' share in claims paid (see Note 7)	3 824 769	1 252 298
Reinsurers' share in changes in outstanding claims reserves (see Note 8)	38 948 278	1 474 386
Reinsurance commission income (see Note 6)	264 867	206 621
Net result of ceded reinsurance activities:	**39 857 414**	**235 823**

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

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

PZU Centrum Operaciji SA 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

	2018	2017
POWSZECHNY ZAKŁAD UBEZPIECZEŃ S.A. (PZU):		
Reinsurance Premiums ceded	(2 585 307)	(1 867 632)
Change in reinsurers' share in unearned premium reserves	200 031	187 136
Reinsurers' share in claims paid	1 123 526	263 169
Change in reinsurers' share in outstanding claims reserves	41 774 526	429 818
Reinsurance Commissions	189 754	149 293
	40 702 530	**(838 216)**

	2018	2017
Lietuvos Draudimas AB:		
Fronting insurance premiums	(389 636)	(420 382)
Commissions from insurance policies fronting	23 849	22 215
Fronting insurance claims	1 488 526	163 209
Change of fronting insurance unearned premium reserves	(28 123)	130 309
Change of fronting insurance deferred client acquisition costs	1 486	(10 046)
Change of fronting insurance outstanding claims reserves	(1 422 743)	1 433 986
	(326 641)	**1 319 291**

Other transactions

	2018	2017
Lietuvos Draudimas AB:		
Investment portfolio management services	(50 600)	(6 724)
Indemnity costs, claim handling fee and subrogations	(99 971)	(161 871)
Indemnity costs, claim handling fee and subrogations	72 591	57 713
	(77 980)	**(110 882)**

	2018	2017
POWSZECHNY ZAKŁAD UBEZPIECZEŃ S.A. (PZU):		
Accrued interest and amortisation for subordinated loan	(60 975)	(121 560)
Indemnity costs, claim handling fee and subrogations	(191 936)	(144 262)
Indemnity costs, claim handling fee and subrogations	60 043	101 632
	(192 868)	**(164 190)**

	2018	2017
Lietuvos Draudimas AB Estonia branch:		
Indemnity costs, claim handling fee and subrogations	-	(150)
Indemnity costs, claim handling fee and subrogations	6 828	6 732
	6 828	**6 582**

Notes to the Financial Statements (All amounts in euros)

	2018	2017
PZU Lietuva Gyuybes Draudimas UAB:		
Other services	(4 522)	-
	(4 522)	**-**

	2018	2017
PZU Centrum Operaciji:		
Other services	(11 942)	(14 501)
	(11 942)	**(14 501)**

Balances with related parties

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

	31.12.2018	31.12.2017
POWSZECHNY ZAKŁAD UBEZPIECZEŃ S.A. (PZU):		
Subordinated loan	(2 085 897)	(2 085 828)
Reinsurer's share in unearned premium reserves	(737 694)	(537 663)
Reinsurance payables	(476 025)	(322 156)
Total payables	**(3 299 616)**	**(2 945 647)**
Other receivables	81 088	99 339
Reinsurer's share in outstanding claims reserves	42 257 694	483 168
Unearned reinsurance commissions reserves	265 092	189 524
Reinsurance receivables	834 253	230 506
Other (prepayments)	4 344	-
Total receivables	**43 442 471**	**1 002 537**
	40 142 855	**(1 943 110)**
Lietuvos Draudimas AB:		
Other payables	(50 600)	(48 315)
Fronting insurance reinsurer's share in unearned premium reserves	(162 033)	(190 157)
Fronting insurance payables	(153 982)	(159 768)
Total payables	**(366 615)**	**(398 240)**
Fronting insurance reinsurer's share in outstanding claims reserves	55 095	1 477 838
Unearned fronting insurance commissions reserves	8 560	10 046
Fronting insurance receivables	30 516	9 711
Other receivables	4 350	22 061
Total receivables	**98 521**	**1 519 656**
	(268 094)	**1 121 416**
Lietuvos Draudimas AB Estonia branch:		
Other receivables	-	139
	-	**139**
PZU Lietuva Gyuybes Draudimas UAB:		
Other assets (prepayments)	-	4 487
	-	**4 487**
Total payables	(3 666 231)	(3 343 887)
Total receivables	43 540 992	2 526 819
Net receivables	**39 874 761**	**(817 068)**

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.

Notes to the Financial Statements (All amounts in euros)

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 were not changed as a result of this partial repayment.

	Note	Subordinated loan
As at 1 January 2018		**2 085 828**
Changes from financing cash flows		
Repayment of borrowings		-
Interest paid		(60 906)
Total changes from financing cash flows		**(60 906)**
Liability-related other changes		
Accrued interest and amortisation	15	60 975
Total liability-related other changes		**60 975**
As at 31 December 2018		**2 085 897**

	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**

b) Management remuneration

In 2018, the Company paid remuneration, including compulsory state social security contributions, to the Management Board in the amount of EUR 943 thousand (2017: EUR 998 thousand) and to the Supervisory Board in the amount of EUR 17 thousand (2017: EUR 50 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 2018 there were 25 (31.12.2017: 28) pending cases of litigation versus the Company for a total of EUR 1 137 thousand (31.12.2017: EUR 1 767 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 2018.

The Company does not have any non-cancellable operating leases as at 31 December 2018, 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 2018 amounts to EUR 48 thousand (31.12.2017: EUR 50 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.

<u>Concentration by industry</u>

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.

<u>Reinsurance contract assets</u>

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.

<u>Sensitivity to insurance risk</u>

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 31.12.2018:

	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	1 155 220	(1 155 220)	22 957	(22 957)
Property	14 483	(14 483)	6 282	(6 282)
Motor own damage	11 997	(11 997)	10 776	(10 776)
General TPL	92 229	(75 725)	5 062	(5 062)
Health	85 587	(85 587)	1 718	(1 718)

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):

Year 2018	**Latvia**	**Other OECD countries**	**Other countries**	**Total**
Financial assets and reinsurers' share of claims reserves				
Financial investments at fair value through profit or loss	-	4 771	-	4 771
Financial investments at fair value through other comprehensive income	19 022	55 266	9 054	83 342
Insurance and reinsurance debtors	17 517	996	-	18 513
Reinsurers' share in outstanding claims reserves	-	43 386	-	43 386
Cash and cash equivalents	6 671	-	-	6 671
Other debtors	660	130	-	790
Total financial assets and reinsurers' share of claims reserves	**43 870**	**104 549**	**9 054**	**157 473**
Financial liabilities and claims reserves				
Gross outstanding claims reserves	(75 469)	-	-	(75 469)
Financial liabilities (short-term part)	(9 390)	(876)	-	(10 266)
Financial liabilities (long-term part)	(1 585)	(2 086)	-	(3 671)
Total financial liabilities and claims reserves	**(86 444)**	**(2 962)**	**-**	**(89 406)**
Net position as at 31 December 2018	**(42 574)**	**101 587**	**9 054**	**68 067**

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
Available for sale financial investments	5 021	7 255	9 611	21 887
Held to maturity 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**

Reinsurance coverage

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:

	2018	2017
Personal accident & Travel medical expense	95 903	90 416
Cargo insurance	350 000	350 000
Hull, CMR Property	350 000	350 000
Property insurance	719 269	678 119
General TPL insurance	359 635	339 060
Bonds and guarantees	479 513	452 080
Obligatory Motor TPL	400 000	400 000

In 2018 and 2017, there is no reinsurance coverage for Motor own damage under excess of loss reinsurance agreements.

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. If the liability adequacy test shows a deficiency in the carrying amount of liabilities, the deficiency is recognised as loss for the financial year by recognizing unexpired risk reserve.

Unexpired risk reserve as at 31 December 2018 amounts to EUR 71 000 (31 December 2017: EUR 0).

40. FINANCIAL RISK MANAGEMENT

Risk management system:

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 counterparty default 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.

Notes to the Financial Statements (All amounts in euros)

40.1 Counterparty default risk

The Company takes on exposure to counterparty default 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 counterparty default 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

	31.12.2018	**31.12.2017**
Lithuanian government debt securities	30 002 375	13 538 146
Latvian government debt securities	17 978 040	12 407 703
Polish government debt securities	17 895 907	18 191 907
Bulgarian government debt securities	3 154 621	3 145 894
Croatian government debt securities	3 015 595	3 021 616
Romanian government debt securities	2 883 136	2 932 169
Hungarian government debt securities	1 876 442	1 970 195
Slovenian government debt securities	-	623 630
Corporate bonds	6 535 421	6 520 446
Investment funds	4 770 691	4 906 448
Cash and cash equivalents	6 671 043	4 111 878
	94 783 271	**71 370 032**
Reinsurers' share in unearned premium reserves	965 770	1 146 350
Outstanding claims reserve, reinsurers' share	43 386 057	4 437 779
Reinsurance debtors	996 113	532 913
Receivables due from policyholders	16 407 472	14 486 850
Receivables due from intermediaries	1 109 495	1 003 742
Other receivables	789 921	935 082
	63 654 828	**22 542 716**
Maximum credit exposure, total	**158 438 099**	**93 912 748**

b) Reinsurance risk breakdown by key counterparties

Reinsurer	31.12.2018 Assets related to reinsurance	Rating*	31.12.2017 Assets related to reinsurance	Rating*
Powszechny Zakład Ubezpieczeń SA	43 829 642	**A-**	1 251 336	**A-**
ALD Re Designated Activity Company	368 709	**NR**	662 292	**NR**
Lietuvas Draudimas	247 645	**NR**	1 677 705	**NR**
Swiss Re Group	234 194	**AA-**	613 990	**AA-**
Munich Re Group	148 548	**AA-**	559 031	**AA-**
GeneralRensurance AG	110 000	**AA+**	292 580	**AA+**
Lloyd`s Syndicate 1225 AES	100 000	**A**	100 000	**A**
Hannover Re	89 522	**AA-**	324 828	**AA-**
Royal & Sun Alliance Insurance PLC	55 158	**A**	45 475	**A**
SCOR Global P&C	42 839	**AA-**	137 692	**AA-**
Caisse Centrale de Reassurances	39 419	**AA**	144 485	**AA**
Odyssey America Reinsurance Corporation	23 419	**A-**	61 399	**A-**
ACE Tempest Re Europe	20 000	**AA-**	79 128	**AA-**
Liberty Syndicate, Cologne	20 000	**A**	79 128	**A**
R + V Versicherung AG	17 129	**AA-**	37 740	**AA-**
Lloyd`s Syndicate 2007 NVA	718	**A+**	2 101	**A+**
Transatlantic Reinsurance Company	530	**A+**	1 553	**A+**
Catlin Insurance Company	468	**A+**	1 370	**A+**
Sirius International Insurance Corporation	-	**A-**	29 499	**A-**
Atradius Reinsurance Limited	-	**A**	12 197	**A**
Nationale Borg Reinsurance N.V.	-	**A**	1 791	**A**
Polish Reinsurance Company	-	**A-**	1 722	**A-**
Reinsurance risk	**45 347 940**		**6 117 042**	

* 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):

31 December 2018	**Rated AAA**	**AA**	**A**	**BB**	**BBB**	**Total**
Government bonds	-	-	65 876	3 016	7 914	76 806
Corporate bonds	-	-	-	1 011	5 525	6 536
Investment funds	-	-	1 023	-	3 748	4 771
Total investment assets	**-**	**-**	**66 899**	**4 027**	**17 187**	**88 113**

31 December 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**

40.2 Liquidity risk

The Company is exposed to regular calls on its available cash resources from claims settlements. Liquidity risk is managed according to the rules defined in Market risk and Liquidity risk management policy.

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):

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

Year 2018	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	4 771	-	-	-	4 771
Financial investments at fair value through other comprehensive income	-	4 137	53 710	25 495	83 342
Insurance and reinsurance debtors	-	18 513	-	-	18 513
Reinsurers' share in outstanding claims reserves	-	28 880	9 308	5 198	43 386
Cash and cash equivalents	6 671	-	-	-	6 671
Other debtors	5	694	91	-	790
Total financial assets and reinsurers' share of claims reserves	**11 447**	**52 224**	**63 109**	**30 693**	**157 473**
Financial liabilities and claims reserves					
Gross outstanding claims reserves	-	(46 706)	(16 346)	(12 417)	(75 469)
Financial liabilities	-	(10 266)	(3 579)	(92)	(13 937)
Total financial liabilities and claims reserves	**-**	**(56 972)**	**(19 925)**	**(12 509)**	**(89 406)**
Net position as at 31 December 2018	**11 447**	**(4 748)**	**43 184**	**18 184**	**68 067**

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**

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, 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:

	2018	2017
Latvian government debt securities	0.10%	0.30%
Bulgarian government debt securities	0.01%	0.07%
Croatian government debt securities	0.03%	0.14%
Hungarian government debt securities	0.00%	0.00%
Lithuanian government debt securities	0.13%	0.33%
Polish government debt securities	0.11%	0.46%
Romanian government debt securities	0.01%	0.13%
Slovenian government debt securities	-	0.01%
Corporate bonds	0.08%	0.51%
Investment funds	1.71%	2.41%

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

		2018 EUR	2017 EUR
Market interest rate and impact on fair value	+0.5 percent point	(1 565 914)	(1 405 034)
	-0.5 percent point	1 288 529	1 250 511

b) Fair value determination

Financial assets and financial liabilities other than those reflected at their fair value (see Note 21 and Note 23), 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 2018	**USD**	**EUR**	**GBP**	**PLN**	**Other**	**Total**
Financial assets and reinsurers' share of claims reserves						
Financial investments at fair value through profit or loss	-	4 771	-	-	-	4 771
Financial investments at fair value through other comprehensive income	-	83 342	-	-	-	83 342
Insurance and reinsurance debtors	-	18 513	-	-	-	18 513
Reinsurers' share in outstanding claims reserves	-	39 615	-	3 771	-	43 386
Cash and cash equivalents	102	6 510	-	59	-	6 671
Other debtors	-	790	-	-	-	790
Total financial assets and reinsurers' share of claims reserves	**102**	**153 541**	**-**	**3 830**	**-**	**157 473**
Financial liabilities and claims reserves						
Gross outstanding claims reserves	(39)	(71 078)	(4)	(4 186)	(162)	(75 469)
Financial liabilities	-	(13 937)	-	-	-	(13 937)
Total financial liabilities and claims reserves	**(39)**	**(85 015)**	**(4)**	**(4 186)**	**(162)**	**(89 406)**
Net position as at 31 December 2018	**63**	**68 526**	**(4)**	**(356)**	**(162)**	**68 067**

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

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 MANAGEMENT

Starting from 1 January 2016, the Solvency II regime has come into force. According to this, the Company has established a Capital Management Policy 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):

	2008 and prior	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**Total**
Net claims provisions at end of accident year and cumulative incurred claims in subsequent years												
At end of accident year	16 753	10 106	7 349	5 951	6 411	7 787	8 457	11 114*	10 896*	13 565	18 631	
1 year later	16 327	8 181	5 771	4 683	4 913	6 679	8 357*	9 115*	8 646*	11 693		
2 years later	15 046	7 977	5 511	4 386	4 999	6 798*	8 189*	8 709*	8 607*			
3 years later	13 417	7 999	5 263	4 757	4 850	6 560*	7 668*	9 268*				
4 years later	12 350	7 971	5 418	4 804	4 745	6 170*	7 591*					
5 years later	11 377	8 019	5 452	4 510	4 434	6 017*						
6 years later	11 116	7 879	5 132	4 595	4 537							
7 years later	11 040	7 871	5 105	4 600								
8 years later	10 961	7 956	5 040									
9 years later	10 960	8 075										
10 years later	11 439											
Net claims paid												
1 year later	7 366	5 945	3 933	3 546	3 772	4 880	5 888*	6 054*	5791*	6 836	-	
2 years later	617	359	77	279	390	238*	440*	614*	287			
3 years later	387	426	67	411	104	208*	330*	195*				
4 years later	440	53	962	39	9	262*	84*					
5 years later	63	112	72	132	96	30*						
6 years later	409	137	-26	5	-7							
7 years later	150	450	-22	99								
8 years later	94	190	-37									
9 years later	131	4										
10 years later	42											
Cumulative net claims paid	**9 699**	**7 676**	**5 026**	**4 511**	**4 364**	**5 618***	**6 742***	**6 863***	**6 078***	**6 836**	**-**	**63 413***
CY (deficiency) / redundancy	**-479**	**-119**	**65**	**-5**	**-103**	**153****	**77****	**-559****	**39****	**1 872****	**-**	**941****

*) 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

BALTA has received Anna Teresa Mank's notice of resignation from the position of the Supervisory Board Member of BALTA as of 26 February 2019. BALTA Supervisory Board will operate in an incomplete four members composition until the respective decision of the Shareholders' meeting. The changes have been registered in the Commercial Register of the Republic of Latvia on 8 March 2019.

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.

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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 51 of the accompanying Annual Report, which comprise:

- the statement of financial position as at 31 December 2018,
- the statement of comprehensive income for the year then ended,
- the statement of changes in shareholders' 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 2018, 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 2018 amounted to EUR 75 469 058 (31 December 2017: EUR 26 361 933). The change in gross outstanding claims reserves in 2018 amounted to EUR 49 107 125 (increase) (in 2017: EUR 3 903 185 (increase)).

Reference to the financial statements: Note 2.3 h) "Insurance contract liabilities" and Note 3 (accounting policy); Note 8 "Outstanding claims reserves" (Notes to the financial statements).

Key audit matter

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 within liabilities in the statement of financial position. The most significant claims reserves are associated with the obligatory property insurance, motor third party liability and motor own damage 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 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 material 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, expected court settlements, discount rates, changes in the amount of future annuity payments, and the expected payment period.

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

Our response

Our audit procedures, performed, where applicable, with the assistance of our actuarial and information technology (IT) specialists, included, among others:

- Testing the design, implementation and operating effectiveness of key controls related to the process of establishing and remeasuring outstanding claims reserves, including the relevant management review controls, accounting and actuarial controls, such as reconciliations of key data underlying the actuarial calculations (including 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 settlement, 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.

underlying the actuarial projections was also our area of audit focus. Due to the above factors, we considered measurement of the non-life insurance outstanding claims reserves to be our key audit matter.	• For all insurance contract portfolios, performing a retrospective analysis of 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 current actuals, and seeking Management Board's explanations for any significant differences. • For all significant insurance contract portfolios, such as, among others, property, obligatory motor third party liability and motor own damage, 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 2018. Our total uninterrupted period of engagement is 6 years, covering the periods ending 31 December 2013 to 31 December 2018.

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
15 March 2019

Inga Lipšāne
Latvian Certified Auditor
Certificate No. 112