Reputation Risk

Reputation risk is a risk that customers of the Bank, its counterparties, shareholders, supervisory bodies or other stakeholders can form a negative opinion about the Bank, which may affect ability of the Bank to maintain existing business relationships and create new ones with customers and other counterparties.

Structure and organization of the risk management function

Management of reputation risk is regulated by the Reputation Risk Management Policy. The risk management system consists of the following steps:

- identification and assessment of a possible Bank’s reputation risks;
- monitoring of Bank’s reputation risks (studying, reporting, assessment, preparation of communication documents, etc.);
- reputation risk management;
- determining of measures that are to be implemented if some negative information poses a threat to Bank’s reputation (risk mitigation measures).

Risk measurement and assessment methods

Reputation risk cannot be determined in terms of quantity. It is very difficult to determine risk consequences and damage in case it occurs. Reputation risk is closely related to operational risks (including legal) and is not always possible to separate them.

Reputation risk is measured within the scope of significant business processes and identification of significant risks. Reputation risk is measured by the Risk Assessment Working Group of Experts on the basis of questionnaires developed for risk assessment of significant products.

Risk assessment is performed based on the following criteria:
- quality of Bank’s products and customer service process (customers’ complaints, shortcomings identified as a result of monitoring of operational risk);
- safety and quality of Bank’s technologies (Internet, Telephone, etc.);
- presence of negative information in mass media and rumours about the Bank or persons associated with the Bank;
- actions of third parties which may result in Bank’s involvement in fraudulent transactions.

As a result of risk assessment, those Bank’s business processes and products are defined which have the greatest exposure to reputational risk.

Methodology used by the Bank for risk mitigation

Depending on the risk nature (internal, external or mixed risks), the action and objectives of the Bank regarding these risks are set as follows:

<table>
<thead>
<tr>
<th>Reputation risk group</th>
<th>Objectives</th>
</tr>
</thead>
<tbody>
<tr>
<td>Internal risks</td>
<td>Eliminate risks</td>
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<tr>
<td>Internal-external risks</td>
<td>To the extent possible, eliminate or minimize risks</td>
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<tr>
<td>External risks</td>
<td>To the extent possible, apply measures to minimize risks</td>
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The activities of the Bank are regulated by a range of policies, procedures and other normative documents specified by the Bank which, while performing other functions, also provide for Bank’s reputation risk mitigation and elimination.

- The following steps are taken in the Bank to mitigate reputation risk:
  - ongoing control of compliance with requirements set in legislation of the Republic of Latvia and by the regulatory bodies;
  - the payment discipline is strictly observed, including timely execution of customers’ payment orders, timely payout of deposit principal and interest, etc.;
  - control of reporting dates, as well as credibility and accuracy of any other information intended for publication;
  - ongoing monitoring of information in mass media that can hurt Bank’s reputation.

The control of compliance of risk management policies and procedures, distribution of duties, powers and responsibilities in risk management, established order for decision making and reporting, and procedure for information exchange – these are general measures for risk mitigation.

The Bank provides regular monitoring of the identified reputation risk inherent in its main products, types of activities, processes and systems to timely mitigate any impact of a contingent risk on activities of the Bank.

All units of the Bank within their competence oversee any occurrence of reputational risk events and perform monitoring of reputational risk in accordance with the risk groups (internal, external or mixed type of risks) set out in the Reputation Risk Management Policies.

All units of the Bank identify and timely report on any reputational risk events in their field of activities.

If an event is determined which may result in the bank’s reputational risk, the relevant unit immediately - as soon as the risk has been established provides information to the Risk Director, who performs assessment of the significance of supplied information to set measures for its management. There may be a decision taken for further observation of the risk or for elimination the risk and/or crisis plan preparation.

Units within which the events are identified which may cause reputational risk have to report thereof to the Risk Control Division at least once a quarter.

The Risk Control Division provides registration of supplied information in the Reputation Risk Event Registration Database and once a quarter provides information to the Risk Director about the events recorded in the Database.

The Risk Director combines and evaluates the information contained in the Database and on a quarterly basis (or more often, if required) provides information to the Board on the magnitude of the risk.