

# **AS LATVIJAS BALZAMS**

ANNUAL ACCOUNTS  
FOR THE YEAR ENDED  
31 DECEMBER 2006

Translation from Latvian original

**AS LATVIJAS BALZAMS**  
**ANNUAL ACCOUNTS FOR THE YEAR ENDED 31 DECEMBER 2006**

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**ANNUAL ACCOUNTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**THE MANAGEMENT**

Names and positions of Council members

Alexander Kovalev – Chairman of the Council

Pjotr Aven – Member of the Council

Vitolds Kokars – Deputy Chairman of the Council  
Director for quality control of AS Latvijas balzams

Alexey Oliynik – Member of the Council

Yury Shefler – Member of the Council until 22 April 2006

Juris Gulbis – Member of the Council until 23 October 2006

Andrejs Skurihins – Member of the Council until 22 April 2006

Names and positions of Board members

Rolands Gulbis – Chairman of the Board  
General director of AS Latvijas balzams

Alexander Yernev – Member of the Board  
Chief engineer of AS Latvijas balzams

Egils Dzerelis – Member of the Board  
Director of logistics of AS Latvijas balzams

Sergey Limarenko – Member of the Board  
Chief of internal security department of AS Latvijas balzams

Valizhan Abidov – Member of the Board

**AS LATVIJAS BALZAMS**  
**ANNUAL ACCOUNTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**MANAGEMENT'S REPORT**

**Type of operations**

AS Latvijas balzams (hereinafter the Company) is the largest producer of alcoholic beverages in the Baltics, which produces more than 120 different types of drinks.

**Performance of the Company during the reporting year**

Year 2006 has been a successful year for the Company because the objectives for 2006 have been fulfilled. Turnover of the Company was 58.9 million Lats (83.9 million EUR), profit for the reporting year was 2.6 million Lats (3.7 million EUR). The increase in turnover was 5% in comparison with the same period in 2005. There has been a considerable increase in export sales. In comparison with 2005 there has been a 26% or 6.5 million Lats (9.2 million EUR) increase in export sales. The main export places were the Baltic States, Poland and Scandinavia. Simultaneously active search for new export markets has been performed and sales of goods have been started in 3 new countries – Kirghizia, Finland and China. In the beginning of the year sales in Ferry boat shops have been launched and it has been a success.

Profit in the reporting year has been influenced by increase in advertising and marketing as well as administrative expenses, which is explained by activities in the Baltic States and positioning in new export markets as well as the general tendencies in the economy.

In 2006 AS Latvijas balzams has contributed 42.5 million Lats (60.5 million EUR) as taxes into the State budget, including 31.6 million Lats (45,0 million EUR) as excise tax.

The average number of employees in 2006 was 779 with an average monthly gross salary of 520 Lats (740 EUR).

**Distribution of profit proposed by the Board**

The Board proposes to distribute part of the profit for year 2006 in dividends, proposing to pay 0.024 Lats (0.034 EUR) per share. The remaining part of current profit is to be retained as retained earnings.

**Future prospects**

The main priority of AS Latvijas balzams for the year 2007 will be promotion of export sales. At the same time, the Company plans to keep its leading position in the local market.

**The Management**

There have been changes in the composition of the Management in 2006. For the list of the Management please see page 3.

**Responsibility of the Management about financial statements**

The Management is responsible for the preparation of the financial statements in accordance with International Financial Reporting Standards as adopted the EU. The financial statements give a true and fair view of the financial position of the Company at the end of the reporting year, and the results of its operations and cash flow for the year then ended.

The Management confirms that the 2006 financial statements on pages 8 to 37 have been prepared using prudent and reasonable judgements and estimates. The accounting policies applied have been consistent except for the accounting of land at revalued amount. The Management confirms that the financial statements have been prepared on going concern basis.

The Management is responsible for accounting records and for safeguarding the Company's assets and preventing and detecting of fraud and other irregularities in the Company. It is also responsible for operating the Company in compliance with the legislation of the Republic of Latvia.

**AS LATVIJAS BALZAMS**  
**ANNUAL ACCOUNTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**MANAGEMENT'S REPORT** (continued)

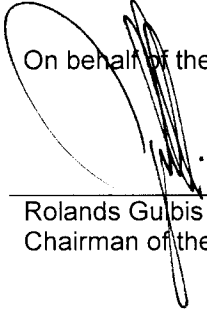
**Significant post balance sheet events**

During the period between the last day of the financial year and the date of signing of this report there have been no significant events that would have a material effect on the year-end results.

**Auditors**

The audit of the financial statements included on pages 8 to 37 was performed by the audit firm PricewaterhouseCoopers SIA in accordance with International Standards on Auditing.

On behalf of the Management of AS Latvijas balzams:

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Rolands Gulbis  
Chairman of the Board

Riga, 12 April 2007

## INDEPENDENT AUDITORS' REPORT

### **To the Shareholders of AS Latvijas balzams**

#### **Report on the Financial Statements**

We have audited the accompanying financial statements on pages 8 to 37 of AS Latvijas balzams which comprise the balance sheet as of 31 December 2006 and the income statement, statement of changes in equity and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory notes.

#### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the requirements of International Financial Reporting Standards as adopted by the European Union. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

#### *Auditor's Responsibility*

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

*Basis for qualified opinion*

The Company's accounting policy is to account for buildings at revalued amounts less subsequent depreciation. The Company performed a revaluation of buildings in 2005 and accounted for the revaluation effect as of 1 September 2005. The previous revaluation was performed on 1 January 1998. International Accounting Standard 16, *Property, Plant and Equipment*, provides that the revaluations should be made with sufficient regularity such that the carrying amount does not differ materially from that which would be determined using fair value at the balance sheet date. Considering the general increase in real estate prices in the Latvian market over recent years, as well as the result of the revaluation performed as of 1 September 2005 we consider that the fair value of the buildings had changed materially between 1998 and 31 December 2004. Accordingly, we consider that the carrying amount of buildings of Ls 6,361 thousand as of 31 December 2004 was materially lower than their fair value and, consequently, the depreciation charge for 2005 has been understated. The financial statements do not disclose the fact of existence of the above described material error as at 31 December 2004 as required by International Accounting Standard 8, *Accounting Policies, Changes in Accounting Estimates and Errors*. In the absence of valuation of buildings as at 31 December 2004 we qualified our audit report on the financial statements for the year ended 31 December 2005.

*Qualified opinion*

In our opinion, except for the effects on the corresponding figures for 2005 of the matter referred to above in paragraph *Basis for qualification*, the accompanying financial statements give a true and fair view of the financial position of the Company as of 31 December 2006, and of its financial performance and its cash flows for the year then ended in accordance with the requirements of International Financial Reporting Standards as adopted by the European Union.

**Report on Other Legal and Regulatory Requirements**

We have read the management report set out on pages 4 to 5 and did not identify material inconsistencies between the financial information contained in the management report and that contained in the financial statements for 2006.

PricewaterhouseCoopers SIA  
Certified audit company  
Licence No. 5



Juris Lapshe  
Certified auditor in charge  
Certificate No. 116

Member of the Board

Riga, Latvia  
28 April 2007

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**BALANCE SHEET AS AT 31 DECEMBER 2006**

	Notes	31.12.2006 Ls	31.12.2006 EUR	31.12.2005 Ls	31.12.2005 EUR
<b><u>Assets</u></b>					
<b>Non-current assets</b>					
Property, plant and equipment	3	22,815,965	32,464,193	20,122,993	28,632,439
Intangible assets		9,823	13,977	116,786	166,172
Loans to related parties	27(h)	14,477,762	20,600,000	-	-
		<b>37,303,550</b>	<b>53,078,170</b>	<b>20,239,779</b>	<b>28,798,611</b>
<b>Current assets</b>					
Inventories	5	14,582,063	20,748,406	12,243,986	17,421,622
Trade receivables	6	8,753,504	12,455,114	11,127,988	15,833,700
Receivables from related parties	27(g)	7,646,440	10,879,904	5,076,483	7,223,185
Loans to related parties	27(h)	101,063	143,800	3,031,063	4,312,814
Other current assets	7	674,304	959,448	511,734	728,132
Current income tax		28,348	40,336	-	-
Cash and cash equivalents	8	103,707	147,562	906,186	1,289,387
		<b>31,889,429</b>	<b>45,374,570</b>	<b>32,897,440</b>	<b>46,808,840</b>
<b>Total assets</b>		<b>69,192,979</b>	<b>98,452,740</b>	<b>53,137,219</b>	<b>75,607,451</b>
<b><u>Equity</u></b>					
Share capital	9	7,496,900	10,667,128	7,496,900	10,667,128
Share premium		61,767	87,887	61,767	87,887
Revaluation reserve		12,193,932	17,350,402	5,334,638	7,590,506
Other reserves		-	-	1,249,047	1,777,234
Merger reserve		-	-	(11,101,905)	(15,796,588)
Retained earnings		10,811,497	15,383,374	18,265,462	25,989,411
<b>Total equity</b>		<b>30,564,096</b>	<b>43,488,791</b>	<b>21,305,909</b>	<b>30,315,578</b>
<b><u>Liabilities</u></b>					
<b>Non-current liabilities</b>					
Deferred tax liability	21(c)	2,426,022	3,451,919	1,336,030	1,901,000
Borrowings	10	12,982,523	18,472,466	8,931,808	12,708,818
		<b>15,408,545</b>	<b>21,924,385</b>	<b>10,267,838</b>	<b>14,609,818</b>
<b>Current liabilities</b>					
Borrowings	10	7,097,336	10,098,599	4,752,897	6,762,763
Trade payables		4,658,195	6,628,015	5,914,006	8,414,872
Payables to related parties	27(f)	1,483,715	2,111,136	535,997	762,655
Current income tax		-	-	467,960	665,847
Other payables	11	9,981,092	14,201,814	9,892,612	14,075,918
		<b>23,220,338</b>	<b>33,039,564</b>	<b>21,563,472</b>	<b>30,682,055</b>
<b>Total liabilities</b>		<b>38,628,883</b>	<b>54,963,949</b>	<b>31,831,310</b>	<b>45,291,873</b>
<b>Total equity and liabilities</b>		<b>69,192,979</b>	<b>98,452,740</b>	<b>53,137,219</b>	<b>75,607,451</b>

The Notes on pages 13 to 37 are an integral part of these financial statements.

Rolands Gulbis  
Chairman of the Board  
12 April 2007



**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**INCOME STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2006**

	Notes	2006 Ls	2006 EUR	2005 Ls	2005 EUR
Revenue	13	58,943,083	83,868,451	51,147,347	72,776,118
Cost of sales	14	(47,764,160)	(67,962,277)	(41,060,157)	(58,423,340)
<b>Gross profit</b>		<b>11,178,923</b>	<b>15,906,174</b>	<b>10,087,190</b>	<b>14,352,778</b>
Selling expenses	15	(4,915,005)	(6,993,422)	(3,842,796)	(5,467,806)
Administrative expenses	16	(4,575,172)	(6,509,883)	(4,085,767)	(5,813,523)
Other income	17	2,204,100	3,136,152	1,719,984	2,447,317
Other expenses	18	(75,520)	(107,455)	(379,141)	(539,469)
Finance income	20	574,084	816,848	144,675	205,854
Finance costs	20	(1,226,608)	(1,745,306)	(654,125)	(930,736)
<b>Profit before income tax</b>		<b>3,164,802</b>	<b>4,503,108</b>	<b>2,990,020</b>	<b>4,254,415</b>
Income tax expense	21	(585,983)	(833,779)	(612,344)	(871,287)
<b>Profit for the year</b>		<b>2,578,819</b>	<b>3,669,329</b>	<b>2,377,676</b>	<b>3,383,128</b>
<b>Earnings per share</b> (expressed in santims and euro cents per share)					
– Basic	22	34.40	48.94	31.72	45.13
– Diluted	22	34.40	48.94	31.72	45.13

The Notes on pages 13 to 37 are an integral part of these financial statements.

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2006**

	Share capital Ls	Share premium Ls	Revaluation reserve Ls	Other reserves* Ls	Merger reserve ** Ls	Retained earnings Ls	Total Ls
<b>Balance at</b>							
<b>31 December 2004</b>	<b>7,496,900</b>	<b>61,767</b>	<b>984,878</b>	<b>1,249,047</b>	<b>(11,101,905)</b>	<b>15,886,958</b>	<b>14,577,645</b>
Disposal of revalued property, plant and equipment	-	-	(828)	-	-	828	-
Property, plant and equipment revaluation	-	-	5,118,193	-	-	-	5,118,193
Change in deferred tax liability as a result of revaluation of property, plant and equipment (Note 21c)	-	-	(767,605)	-	-	-	(767,605)
<i>Net income recognized directly in equity</i>	-	-	4,350,588	-	-	-	4,350,588
Profit for the year	-	-	-	-	-	2,377,676	2,377,676
<b>Total recognized income and expense for 2005</b>	<b>-</b>	<b>-</b>	<b>4,349,760</b>	<b>-</b>	<b>-</b>	<b>2,378,504</b>	<b>6,728,264</b>
<b>Balance as at 31 December 2005</b>	<b>7,496,900</b>	<b>61,767</b>	<b>5,334,638</b>	<b>1,249,047</b>	<b>(11,101,905)</b>	<b>18,265,462</b>	<b>21,305,909</b>
Property, plant and equipment revaluation (Note 3)	-	-	8,069,758	-	-	-	8,069,758
Change in deferred tax liability as a result of revaluation of property, plant and equipment (Note 21c)	-	-	(1,210,464)	-	-	-	(1,210,464)
<i>Net income recognized directly in equity</i>	-	-	6,859,294	-	-	-	6,859,294
Profit for the year	-	-	-	-	-	2,578,819	2,578,819
<b>Total recognized income and expense for 2006</b>	<b>-</b>	<b>-</b>	<b>6,859,294</b>	<b>-</b>	<b>-</b>	<b>2,578,819</b>	<b>9,438,113</b>
Dividends for 2005	-	-	-	-	-	(179,926)	(179,926)
Reclassification of merger reserve to retained earnings	-	-	-	-	11,101,905	(11,101,905)	-
Reclassification of other reserves to retained earnings	-	-	-	(1,249,047)	-	1,249,047	-
<b>Balance as at 31 December 2006</b>	<b>7,496,900</b>	<b>61,767</b>	<b>12,193,932</b>	<b>-</b>	<b>-</b>	<b>10,811,497</b>	<b>30,564,096</b>

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

	Share capital EUR	Share premium EUR	Revaluation reserve EUR	Other reserves* EUR	Merger reserve ** EUR	Retained earnings EUR	Total EUR
<b>Balance at</b>							
<b>31 December 2004</b>	<b>10,667,128</b>	<b>87,887</b>	<b>1,401,355</b>	<b>1,777,234</b>	<b>(15,796,588)</b>	<b>22,605,105</b>	<b>20,742,121</b>
Disposal of revalued property, plant and equipment	-	-	(1,178)	-	-	1,178	-
Property, plant and equipment revaluation	-	-	7,282,533	-	-	-	7,282,533
Change in deferred tax liability as a result of revaluation of property, plant and equipment (Note 21c)	-	-	(1,092,204)	-	-	-	(1,092,204)
<i>Net income recognized directly in equity</i>	-	-	6,190,329	-	-	-	6,190,329
Profit for the year	-	-	-	-	-	3,383,128	3,383,128
<b>Total recognized income and expense for 2005</b>	<b>-</b>	<b>-</b>	<b>6,189,151</b>	<b>-</b>	<b>-</b>	<b>3,384,306</b>	<b>9,573,457</b>
<b>Balance as at 31 December 2005</b>	<b>10,667,128</b>	<b>87,887</b>	<b>7,590,506</b>	<b>1,777,234</b>	<b>(15,796,588)</b>	<b>25,989,411</b>	<b>30,315,578</b>
Property, plant and equipment revaluation (Note 3)	-	-	11,482,231	-	-	-	11,482,231
Change in deferred tax liability as a result of revaluation of property, plant and equipment (Note 21c)	-	-	(1,722,335)	-	-	-	(1,722,335)
<i>Net income recognized directly in equity</i>	-	-	9,759,896	-	-	-	9,759,896
Profit for the year	-	-	-	-	-	3,669,329	3,669,329
<b>Total recognized income and expense for 2006</b>	<b>-</b>	<b>-</b>	<b>9,759,896</b>	<b>-</b>	<b>-</b>	<b>3,669,329</b>	<b>13,429,225</b>
Dividends for 2005	-	-	-	-	-	(256,012)	(256,012)
Reclassification of merger reserve to retained earnings	-	-	-	-	15,796,588	(15,796,588)	-
Reclassification of other reserves to retained earnings	-	-	-	(1,777,234)	-	1,777,234	-
<b>Balance as at 31 December 2006</b>	<b>10,667,128</b>	<b>87,887</b>	<b>17,350,402</b>	<b>-</b>	<b>-</b>	<b>15,383,374</b>	<b>43,488,791</b>

\* Other reserves were made before the required re-registration of the Company in the Commercial Register in the amount of 5% from annual profit in accordance with Latvian legal requirements. Since neither the Commercial Law, nor Statutes of the Company now require the creation of such reserves, shareholders have made a decision on transfer of reserves to retained earnings.

\*\* The merger reserve arose as a result of merger of the Company with its subsidiary in 2000. The Company chose to account for the merger in accordance with pooling of interests method. The merger reserve represents the excess of the pre-merger carrying amount of the investment in the subsidiary over the carrying amount of net assets absorbed by the Company as a result of the merger. Shareholders have made a decision on transfer of reserves to retained earnings.

The Notes on pages 13 to 37 are an integral part of these financial statements.

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**CASH FLOW STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2006**

	Notes	2006 Ls	2006 EUR	2005 Ls	2005 EUR
<b>Cash flows from operating activities</b>					
Cash generated from operations	23	2,438,722	3,469,990	6,826,387	9,713,073
Interest paid		(1,042,267)	(1,483,011)	(588,829)	(837,828)
Income tax paid		(1,204,333)	(1,713,611)	(151,810)	(216,006)
<b>Net cash generated from operating activities</b>		<b>192,122</b>	<b>273,368</b>	<b>6,085,748</b>	<b>8,659,239</b>
<b>Cash flows from investing activities</b>					
Purchase of property, plant and equipment		(1,005,404)	(1,430,564)	(3,287,490)	(4,677,677)
Proceeds from sale of property, plant and equipment		4,622,432	6,577,128	15,865	22,574
Loans granted	27(h)	(18,728,371)	(26,648,071)	(3,031,063)	(4,312,814)
Interest received		375,886	534,838	-	-
Loans repayment received		7,080,583	10,074,762	22,000	31,303
<b>Net cash used in investing activities</b>		<b>(7,654,874)</b>	<b>(10,891,907)</b>	<b>(6,280,688)</b>	<b>(8,936,614)</b>
<b>Cash flows from financing activities</b>					
Proceed from borrowings		15,591,726	22,185,027	2,714,150	3,861,888
Dividends paid		(179,926)	(256,012)	-	-
Repayment of borrowings		(8,751,527)	(12,452,301)	(2,510,688)	(3,572,387)
<b>Net cash generated from financing activities</b>		<b>6,660,273</b>	<b>9,476,714</b>	<b>203,462</b>	<b>289,501</b>
<b>Net (decrease) / increase in cash and cash equivalents during the year</b>		<b>(802,479)</b>	<b>(1,141,825)</b>	<b>8,522</b>	<b>12,126</b>
Cash and cash equivalents at beginning of the year		906,186	1,289,387	897,664	1,277,261
<b>Cash and cash equivalents at end of the year</b>	8	<b>103,707</b>	<b>147,562</b>	<b>906,186</b>	<b>1,289,387</b>

The Notes on pages 13 to 37 are an integral part of these financial statements.

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS**

**1 GENERAL INFORMATION**

The Company is the largest producer of alcoholic beverages in the Baltics. At present AS Latvijas balzams produces more than 120 different types of drinks. The largest shareholder of the Company, who owns 88.05% of the shares of the Company, is S.P.I. Distilleries B.V., which is incorporated in Netherlands.

AS Latvijas balzams is joint stock company incorporated and domiciled in Latvia. The Company is incorporated in 1900; however the current name of the Company was created in 1970. The address of its registered office is A. Čaka Street 160, Rīga, LV-1012, Republic of Latvia. Shares of the Company are listed in the Riga Stock Exchange second list.

These financial statements have been approved for issue by the Management on 12 April 2007 and signed on its behalf by the Chairman of the Board Rolands Gulbis.

**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

**(a) Basis of preparation**

The financial statements of AS Latvijas balzams have been prepared in accordance with International Financial Reporting Standards as adopted the EU.

The financial statements have been prepared under the historical cost convention, as modified by the revaluation of property, plant and equipment as disclosed in Note (e).

The preparation of the financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Company's accounting policies. Significant accounting estimates are described in Note (t).

*(a) Standards, amendments and interpretations that are not yet effective and have not been early adopted by the Company*

The following standards and amendments to existing standards have been published that are mandatory for the Company's accounting periods beginning on or after 1 March 2006 or later periods that the Company has not early adopted:

*IFRS 7, Financial Instruments: Disclosures, and a complementary amendment to IAS 1, Presentation of Financial Statements – Capital Disclosures (effective from 1 January 2007).*

IFRS 7 introduces new disclosures to improve the information about financial instruments. It requires the disclosure of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk, including sensitivity analysis to market risk. It replaces IAS 32, Financial Instruments: Disclosure and Presentation. It is applicable to all entities that report under IFRS. The amendment to IAS 1 introduces disclosures about the level of an entity's capital and how it manages capital. The Company assessed the impact of IFRS 7 and the amendments to IAS 1 and concluded that the main additional disclosures will be the sensitivity analysis to market risk and the capital disclosures required by the amendment of IAS 1. The Company will apply IFRS 7 and the amendment to IAS 1 from annual periods beginning 1 January 2007.

*IAS 23, Borrowing Costs, revised (effective from 1 January 2009)*

IAS 23 eliminates of the option of immediate recognition as an expense of borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset. The Company's current accounting policy complies with this amendment.

*IFRS 8, Operating Segments (effective from 1 January 2009).*

IFRS 8 replaces IAS 14 and aligns segment reporting with the requirements of the US standard SFAS 131 Disclosures about Segments of an Enterprise and Related Information. The Company assessed the impact of IFRS 8 and concluded that there are no additional disclosures to be made in the financial statements.

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (continued)

**(a) Basis of preparation** (continued)

*(b) Standards, amendments and interpretations that are mandatory for accounting periods beginning on or after 1 January 2006 but are not relevant to the Company's operations:*

IAS 19	(Amendment)	Employee benefits
IAS 21	(Amendment)	Net Investment in a Foreign Operation
IAS 39	(Amendment)	Cash Flow Hedge Accounting of Forecast Intragroup Transactions
IAS 39	(Amendment)	The Fair Value Option
IAS 39 and IFRS 4	(Amendment)	Financial Guarantee Contracts
IFRS 1	(Amendment)	First-time Adoption of International Financial Reporting Standards and IFRS 6 (Amendment), Exploration for and Evaluation of Mineral Resources
IFRS 6		Exploration for and Evaluation of Mineral Resources
IFRIC 4		Determining whether an Arrangement contains a Lease
IFRIC 5		Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds
IFRIC 6		Liabilities arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment

*(c) Standards and interpretations to existing standards that are not yet effective and not relevant for the Company's operations*

The following interpretations to existing standards have been published that are mandatory for the Company's accounting periods beginning on or after 1 March 2006 or later periods but are not relevant for the Company's operations:

*IFRIC 7, Applying the Restatement Approach under IAS 29, Financial Reporting in Hyperinflationary Economies (effective from 1 March 2006).*

*IFRIC 8, Scope of IFRS 2 (effective for annual periods beginning on or after 1 May 2006).*

*IFRIC 9, Reassessment of embedded derivatives (effective for annual periods beginning on or after 1 June 2006).*

*IFRIC 10, Interim Financial Reporting and Impairment (effective for annual periods beginning on or after 1 November 2006).*

*IFRIC 11, IFRS 2 – Group and Treasury Share Transactions (effective for annual periods beginning on or after 1 March 2007)*

*IFRIC 12, Service Concession Arrangements (effective for annual periods beginning on or after 1 January 2008)*

IFRIC 10, 11, 12, IFRS 8 and IAS 23 revised have not been yet endorsed by EU.

Accounting policies have been consistent with those used in the previous reporting period except for accounting of land at revalued amount (see Note (e) under Accounting policies and Note 3).

**(b) Segment reporting**

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**(c) Revenue recognition**

The Company's main operation is the production and sale of alcoholic drinks. Revenue represents the total of goods and services sold during the year net of discounts, value added tax and excise tax.

Income from sales of goods in Latvia is recognised when the customer has accepted the goods. Income from the sales of goods outside Latvia is recognised in accordance with the goods delivery terms. Income from penalties is recognised at the moment of receipt. Sales of services are recognised in the accounting period in which the services are rendered.

Interest income and expense are recognised in the income statement for loans issued and received measured at amortised cost using the effective interest rate method.

**(d) Foreign currency translation**

*(a) Functional and presentation currency*

Items included in the financial statements of the Company are measured using the currency of the primary economic environment in which the Company operates ('the functional currency'). The financial statements are presented in Latvian Lats (Ls), which is the Company's functional and presentation currency. In accordance with the requirements of the Riga Stock Exchange all balances are also presented in Euro (EUR). For disclosure purposes the translation into EUR is based on the official exchange rate as set by the Bank of Latvia during period from 1 January 2005 to 31 December 2006 – EUR/LVL (1 EUR = LVL 0.702804).

*(b) Transactions and balances*

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at the year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

The exchange rates of the principal foreign currencies applied by the Company at the balance sheet dates:

	<b>31.12.2006</b>	<b>31.12.2005</b>
	<b>Ls</b>	<b>Ls</b>
USD 1	0.5360	0.5930
EUR 1	0.702804	0.702804

**(e) Property, plant and equipment**

Buildings and structures are shown at fair value, based on periodic valuations by external independent valuers, less subsequent depreciation. Any accumulated depreciation at the date of revaluation is eliminated against the gross carrying amount of the asset, and the net amount is restated to the revalued amount of the asset. Land is shown at fair value, based on periodic valuations by external independent valuers. All other property, plant and equipment is stated at historical cost less accumulated depreciation. Historic costs includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Increases in the carrying amount arising from revaluation of buildings and structures and land are credited to "Revaluation reserve" in shareholders' equity. Decreases that offset previous increases of the same asset (net of deferred tax) are charged against that reserve directly in equity; all other decreases are charged to the income statement.

The revaluation surplus is transferred directly to retained earnings when the surplus is recognised on retirement or disposal of the asset.

Land is not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate their cost or revalued amounts to their residual values over their estimated useful lives, as follows:

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**(e) Property, plant and equipment (continued)**

	<b>Years</b>
Buildings	10-71
Production equipment	2-25
Other equipment and machinery	2-25

The residual values and useful lives of the assets are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The decrease is reflected as expenses in the income statement or recognised in reserves, in case the asset was previously re-valued.

Costs of borrowing to finance assets under construction and other direct charges related to the particular asset under construction are capitalised, during the time that is required to complete and prepare the asset for its intended use, as part of the cost of the asset. Capitalisation of the borrowing costs is suspended during extended periods in which active developments are interrupted.

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the income statement. When revalued assets are sold, the amounts included in "Revaluation reserve" are transferred to retained earnings.

**(f) Intangible assets**

Intangible assets primarily consist of licences and patents. Intangible assets are stated at historical cost less accumulated amortisation. Amortisation commences when the assets are available for use. Intangible assets are amortised using the straight-line method to allocate their cost to their residual values over their estimated useful lives, as follows:

	<b>Years</b>
Licences and patents	3-5

An intangible asset's carrying amount is written down to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use.

**(g) Inventories**

Inventories are stated at the lower of cost and net realizable value. Cost is determined using the weighted average method. Net realisable value is the estimated selling price in the ordinary course of business, less applicable costs to complete and variable selling expenses. When the net realisable value of inventories is lower than their cost, provisions are created to reduce the value of inventories to their net realisable value.

**(h) Impairment of non-financial assets**

All the Company's non-financial assets except land have a finite useful life and are subject to amortisation or depreciation. Assets that are subject to amortisation or depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less cost to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.



**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**(i) Loans and receivables**

Loans and receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of loans and receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of loans and receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the loans and receivables are impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate. The amount of the provision is recognised in the income statement.

**(j) Share capital and dividends**

Ordinary shares are classified as equity. Dividend distribution to the Company's shareholders is recognized as a liability in the Company's financial statements in the period in which the dividends are approved by the Company's shareholders.

**(k) Borrowings**

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Company has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

**(l) Income tax**

Income tax is assessed for the period in accordance with Latvian tax legislation. The tax rate stated by Latvian tax legislation is 15 percent.

**(m) Deferred income tax**

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability settled.

The principal temporary differences arise from different intangible asset amortization and property, plant and equipment depreciation rates, as well as provisions for slow-moving inventory, accruals for unused annual leave and accruals for bonuses. Deferred income tax asset is recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

However, if the deferred income tax arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit nor loss, it is not accounted for.

**(n) Accruals for unused annual leave**

Amount of accrual is determined by multiplying the average wage per one day of employees in the last six months of reporting year by the number of unused holidays at the end of the reporting year.

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**(o) Pension obligations**

The Company pays social security contributions to the state Social Security Fund (the Fund) on behalf of its employees based on the defined contribution plan in accordance with the local legal requirements. A defined contribution plan is a plan under which the Company pays fixed contributions into the Fund and will have no legal or constructive obligations to pay further contributions if the Fund does not hold sufficient assets to pay all employees benefits relating to employee service in the current and prior period. The social security contributions are recognized as an expense on an accrual basis and are included within staff costs.

**(p) Operating leases - the Company as a lessor**

Assets that are leased out under operating lease terms are recorded within fixed assets at historic cost or revaluated amount less depreciation. Depreciation is calculated on a straight-line basis to write down each asset to its estimated residual value over its estimated useful life using rates set for similar Company's assets. Rental income from operating lease including advances received is recognised on a straight-line basis over the period of the lease.

**(q) Cash and cash equivalents**

Cash and cash equivalents comprise cash in hand and deposits held at call with banks.

**(r) Related parties**

Related parties are defined as the Company's parent company, members of the Board and the Council, their close relatives and companies in which they have a significant influence or control. Related parties are also all companies controlled by the ultimate controlling party or companies where the ultimate controlling party has significant influence.

**(s) Earnings per share**

Earnings per share is determined by dividing the profit or loss attributable to equity holders of the Company by the weighted average number of participating shares outstanding during the reporting year.

**(t) Critical estimates and judgements**

The preparation of the financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Company's accounting policies.

IFRS requires that in preparing the financial statements, management of the Company make estimates and assumptions that affect the reported amounts of assets and liabilities and required disclosure at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The areas involving a higher degree of judgement are revaluation of property, plant and equipment, determination of frequency of revaluations, the management assumptions and estimates in determination of useful lives of property, plant and equipment, recoverable amount of accounts receivable and inventories as described in respective notes.

*Revaluation of property, plant and equipment*

The management determines fair value and the remaining useful life of property, plant and equipment based on valuations performed by independent certified valuers in accordance with real estate valuation standards and based on the average construction costs relevant for the reporting year.

The management considers that the revaluation of property, plant and equipment is to be performed at least each five years.

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (continued)

**(t) Critical estimates and judgements** (continued)

*Recoverable amount of trade receivables*

The estimated collectibility of accounts receivable is assessed on an individual basis for each customer. In case individual assessment is not possible due to the large number of individual balances, only the significant debtors are assessed individually. Receivables that are not individually assessed for impairment are classified into groups of receivables with similar credit risk characteristics and are collectively assessed for impairment, using historical loss experience. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently.

*Inventory valuation*

Upon valuation of inventories, the management will rely on its best knowledge taking into consideration historical experience, general background information and potential assumptions and conditions of future events. In determining the impairment of inventories, the sales potential as well as the net realisable value of inventory are taken into account.

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**3 PROPERTY, PLANT AND EQUIPMENT**

	Land and buildings  Ls	Equipment and machinery  Ls	Other assets  Ls	Assets under construction  Ls	Advances for assets  Ls	Total  Ls
<b>At 1 January 2005</b>						
Cost or valuation	8,859,568	11,160,801	3,087,810	270,553	423,636	23,802,368
Accumulated depreciation	(1,394,804)	(7,454,889)	(2,039,081)	-	-	(10,888,774)
<b>Net book amount</b>	<b>7,464,764</b>	<b>3,705,912</b>	<b>1,048,729</b>	<b>270,553</b>	<b>423,636</b>	<b>12,913,594</b>
<b>Year ended 31 December 2005</b>						
Opening net book amount	7,464,764	3,705,912	1,048,729	270,553	423,636	12,913,594
Additions	-	-	114,339	42,931	3,764,664	3,921,934
Disposals	(112,094)	(2,773)	(909)	-	-	(115,776)
Reclassified from advance payments	278,460	215,422	195,419	2,879,405	(3,568,706)	-
Reclassification	-	122,967	6,754	(129,721)	-	-
Revaluation surplus, net	5,000,766	-	-	-	-	5,000,766
Depreciation charge	(406,955)	(884,940)	(305,630)	-	-	(1,597,525)
<b>Closing net book amount</b>	<b>12,224,941</b>	<b>3,156,588</b>	<b>1,058,702</b>	<b>3,063,168</b>	<b>619,594</b>	<b>20,122,993</b>
<b>At 31 December 2005</b>						
Cost or valuation	12,481,642	11,352,060	3,316,434	3,063,168	619,594	30,832,898
Accumulated depreciation	(256,701)	(8,195,472)	(2,257,732)	-	-	(10,709,905)
<b>Net book amount</b>	<b>12,224,941</b>	<b>3,156,588</b>	<b>1,058,702</b>	<b>3,063,168</b>	<b>619,594</b>	<b>20,122,993</b>
<b>Year ended 31 December 2006</b>						
Opening net book amount	12,224,941	3,156,588	1,058,702	3,063,168	619,594	20,122,993
Additions	-	-	-	-	993,856	993,856
Revaluation surplus, net	8,069,758	-	-	-	-	8,069,758
Disposed and sold	(841,769)	(3,978)	(123,913)	(3,567,569)	-	(4,537,229)
Reclassification	179,893	270,937	252,641	826,551	(1,530,022)	-
Depreciation charge	(774,278)	(744,878)	(314,257)	-	-	(1,833,413)
<b>Net book amount</b>	<b>18,858,545</b>	<b>2,678,669</b>	<b>873,173</b>	<b>322,150</b>	<b>83,428</b>	<b>22,815,965</b>
<b>At 31 December 2006</b>						
Cost or valuation	19,889,525	11,312,992	3,361,012	322,150	83,428	34,969,107
Accumulated depreciation	(1,030,980)	(8,634,323)	(2,487,839)	-	-	(12,153,142)
<b>Net book amount</b>	<b>18,858,545</b>	<b>2,678,669</b>	<b>873,173</b>	<b>322,150</b>	<b>83,428</b>	<b>22,815,965</b>

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**3 PROPERTY, PLANT AND EQUIPMENT (continued)**

	Land and buildings EUR	Equipment and machinery EUR	Other assets EUR	Assets under construction EUR	Advances for assets EUR	Total EUR
<b>At 1 January 2005</b>						
Cost or valuation	12,606,030	15,880,389	4,393,558	384,962	602,780	33,867,719
Accumulated depreciation	(1,984,628)	(10,607,351)	(2,901,351)	-	-	(15,493,330)
<b>Net book amount</b>	<b>10,621,402</b>	<b>5,273,038</b>	<b>1,492,207</b>	<b>384,962</b>	<b>602,780</b>	<b>18,374,389</b>
<b>Year ended 31 December 2005</b>						
Opening net book amount	10,621,402	5,273,038	1,492,207	384,962	602,780	18,374,389
Additions	-	-	162,689	61,085	5,356,634	5,580,408
Disposals	(159,495)	(3,946)	(1,293)	-	-	(164,734)
Reclassified from advance payments	396,213	306,518	278,056	4,097,024	(5,077,811)	-
Reclassification	-	174,966	9,610	(184,576)	-	-
Revaluation surplus, net	7,115,449	-	-	-	-	7,115,449
Depreciation charge	(579,045)	(1,259,156)	(434,872)	-	-	(2,273,073)
<b>Closing net book amount</b>	<b>17,394,524</b>	<b>4,491,420</b>	<b>1,506,397</b>	<b>4,358,495</b>	<b>881,603</b>	<b>28,632,439</b>
<b>At 31 December 2005</b>						
Cost or valuation	17,759,777	16,152,526	4,718,860	4,358,495	881,603	43,871,261
Accumulated depreciation	(365,253)	(11,661,106)	(3,212,463)	-	-	(15,238,822)
<b>Net book amount</b>	<b>17,394,524</b>	<b>4,491,420</b>	<b>1,506,397</b>	<b>4,358,495</b>	<b>881,603</b>	<b>28,632,439</b>
<b>Year ended 31 December 2006</b>						
Opening net book amount	17,394,524	4,491,420	1,506,397	4,358,495	881,603	28,632,439
Additions	-	-	-	-	1,414,129	1,414,129
Revaluation surplus, net	11,482,231	-	-	-	-	11,482,231
Disposed and sold	(1,197,729)	(5,660)	(176,312)	(5,076,193)	-	(6,455,894)
Reclassification	255,965	385,509	359,475	1,176,076	(2,177,025)	-
Depreciation charge	(1,101,699)	(1,059,866)	(447,147)	-	-	(2,608,712)
<b>Net book amount</b>	<b>26,833,292</b>	<b>3,811,403</b>	<b>1,242,413</b>	<b>458,378</b>	<b>118,707</b>	<b>32,464,193</b>
<b>At 31 December 2006</b>						
Cost or valuation	28,300,244	16,096,938	4,782,289	458,378	118,707	49,756,556
Accumulated depreciation	(1,466,952)	(12,285,535)	(3,539,876)	-	-	(17,292,363)
<b>Net book amount</b>	<b>26,833,292</b>	<b>3,811,403</b>	<b>1,242,413</b>	<b>458,378</b>	<b>118,707</b>	<b>32,464,193</b>

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**3 PROPERTY, PLANT AND EQUIPMENT** (continued)

The Company performed revaluation of buildings on 1 September 2005, when the revaluation was performed by independent valuers AS BDO Invest Rīga using the replacement cost method.

As at 30 May 2006 SIA Vērtētāju birojs Aplēse had performed revaluation of land owned by the Company. The value of land after revaluation as at 31.12.2006 is Ls 8,561,513 (12,181,936 EUR). If the land had not been revalued its net book value would be Ls 372,318 (529,761 EUR). The carrying amount of the revalued buildings as at 31 December 2006 is Ls 10,297,032 (14,651,356 EUR) (31.12.2005: Ls 11,011 (15,667 EUR) thousand). If revalued buildings were stated on the historical cost basis, the carrying amount of these buildings as at 31 December 2006 would be Ls 5,996 (8,532 EUR) thousand (31.12.2005: Ls 6,323 (8,997 EUR) thousand).

As at 31 December 2006 the total revaluation surplus represents Ls 14,345,802 (20,412,237 EUR). The revaluation surplus net of applicable deferred tax was credited to "Revaluation reserve" in shareholders' equity.

All property, plant and equipment of AS Latvijas balzams are pledged in accordance with terms of Mortgage and Commercial pledge agreements as security for loans from the credit institutions (see Note 10).

In 2006 loan interest was not capitalized (in 2005 capitalised interest Ls 42,931 (61,085 EUR)).

**4 INTANGIBLE ASSETS**

	Licenses, patents Ls	Licenses, patents EUR
<b>At 1 January 2005</b>		
Cost	1,162,146	1,653,585
Accumulated amortization	(833,180)	(1,185,508)
<b>Net book amount</b>	<b>328,966</b>	<b>468,077</b>
<b>Year ended 31 December 2005</b>		
Opening net book amount	328,966	468,077
Additions	314	447
Amortisation charge	(212,494)	(302,352)
<b>Closing net book amount</b>	<b>116,786</b>	<b>166,172</b>
<b>At 31 December 2005</b>		
Cost	1,162,460	1,654,032
Accumulated amortisation	(1,045,674)	(1,487,860)
<b>Net book amount</b>	<b>116,786</b>	<b>166,172</b>
<b>Year ended 31 December 2006</b>		
Opening net book amount	116,786	166,172
Additions	11,548	16,431
Disposals	(65)	(93)
Amortization charge	(118,446)	(168,533)
<b>Closing net book amount</b>	<b>9,823</b>	<b>13,977</b>
<b>At 31 December 2006</b>		
Cost	1,163,608	1,655,665
Accumulated amortization	(1,153,785)	(1,641,688)
<b>Net book amount</b>	<b>9,823</b>	<b>13,977</b>

All intangible assets of AS Latvijas balzams are pledged in accordance with terms of Mortgage and Commercial pledge agreements as security for loans from the credit institutions (see Note 10).

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**5 INVENTORIES**

	<b>31.12.2006</b>	<b>31.12.2006</b>	<b>31.12.2005</b>	<b>31.12.2005</b>
	<b>Ls</b>	<b>EUR</b>	<b>Ls</b>	<b>EUR</b>
Raw materials and consumables	7,625,761	10,850,480	5,841,165	8,311,229
Inventory in transit	838,069	1,192,465	377,077	536,532
Finished goods and goods for sale	3,726,087	5,301,744	2,898,711	4,124,494
Excise tax stamps	1,712,527	2,436,706	2,389,665	3,400,187
Work-in-progress	679,619	967,011	737,368	1,049,180
	<b><u>14,582,063</u></b>	<b><u>20,748,406</u></b>	<b><u>12,243,986</u></b>	<b><u>17,421,622</u></b>

During 2006 provisions for impairment of inventory were increased by Ls 92,558 (131,698 EUR) (in 2005 decreased by Ls 15,427 (21,951 EUR)). The amount of increased provisions has been included in "Cost of sales" in the income statement. The provisions for impairment as at 31 December 2006 amounted to Ls 616,969 (877,868 EUR) (31.12.2005: Ls 524,411 (746,170 EUR)).

All inventories of AS Latvijas balzams are pledged in accordance with terms of Mortgage and Commercial pledge agreements as security for loans from the credit institutions (see Note 10).

**6 TRADE RECEIVABLES**

Trade debtors	11,193,160	15,926,432	13,448,418	19,135,375
Provisions for impairment of trade debts	<u>(2,439,656)</u>	<u>(3,471,318)</u>	<u>(2,320,430)</u>	<u>(3,301,675)</u>
	<b><u>8,753,504</u></b>	<b><u>12,455,114</u></b>	<b><u>11,127,988</u></b>	<b><u>15,833,700</u></b>

**7 OTHER CURRENT ASSETS**

VAT accepted	42,218	60,071	94,757	134,827
Insurance	66,766	95,000	83,045	118,163
Other deferred expenses	74,701	106,290	22,307	31,740
Receivables for raw materials	250,635	356,621	134,422	191,265
Receivables for services	145,749	207,382	139,064	197,870
Other debtors	94,235	134,084	38,139	54,267
	<b><u>674,304</u></b>	<b><u>959,448</u></b>	<b><u>511,734</u></b>	<b><u>728,132</u></b>

**8 CASH AND CASH EQUIVALENTS**

Cash in hand	47,037	66,928	46,656	66,386
Cash at bank	<u>56,670</u>	<u>80,634</u>	<u>859,530</u>	<u>1,223,001</u>
	<b><u>103,707</u></b>	<b><u>147,562</u></b>	<b><u>906,186</u></b>	<b><u>1,289,387</u></b>

**9 SHARE CAPITAL**

Registered share capital	<b><u>7,496,900</u></b>	<b><u>10,667,128</u></b>	<b><u>7,496,900</u></b>	<b><u>10,667,128</u></b>
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As at 31 December 2006 the total authorised and fully paid share capital consists of 7,496,900 (31.12.2005: 7,496,900) ordinary shares. Nominal value of one share is Ls 1 (1.42 EUR) (31.12.2005: Ls 1 (1.42 EUR)). Bank borrowings are secured by a pledge of all shares owned by the Company's largest shareholder, S.P.I. Distilleries B.V., and any other shares that S.P.I. Distilleries B.V. may acquire in the future (see Note 10).

In year 2006 the Company paid dividends for year 2005 in amount of Ls 179,926 (256,012 EUR) (Ls 0.024 (0.034 EUR) per share). The Company did not pay dividends in year 2005. For 2006 the Board proposes to distribute part of the profit for year 2006 in dividends, proposing to pay 0.024 Lats (0.034 EUR) per share.

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**10 BORROWINGS**

	<b>31.12.2006</b>	<b>31.12.2006</b>	<b>31.12.2005</b>	<b>31.12.2005</b>
	<b>Ls</b>	<b>EUR</b>	<b>Ls</b>	<b>EUR</b>
AS SEB Latvijas Unibanka	2,635,400	3,749,836	3,718,603	5,291,095
AS Hansabanka	10,347,123	14,722,630	5,213,205	7,417,723
<b>Non-current borrowings</b>	<b>12,982,523</b>	<b>18,472,466</b>	<b>8,931,808</b>	<b>12,708,818</b>
AS SEB Latvijas Unibanka	850,000	1,209,441	680,000	967,553
AS Hansabanka	2,188,953	3,114,599	741,250	1,054,704
Credit line	4,058,383	5,774,559	2,991,647	4,256,730
SIA Bravo	-	-	340,000	483,776
<b>Current borrowings</b>	<b>7,097,336</b>	<b>10,098,599</b>	<b>4,752,897</b>	<b>6,762,763</b>
<b>Total borrowings</b>	<b>20,079,859</b>	<b>28,571,065</b>	<b>13,684,705</b>	<b>19,471,581</b>

The carrying amount of borrowings does not materially differ from their fair value.

	<b>2006</b>	<b>2006</b>	<b>2005</b>	<b>2005</b>
	<b>Ls</b>	<b>EUR</b>	<b>Ls</b>	<b>EUR</b>
At the beginning of reporting year	13,684,705	19,471,581	12,619,037	17,955,272
Loans received during the year	15,591,726	22,185,027	2,614,150	3,719,600
Loans repaid during the year	(8,751,527)	(12,452,301)	(2,410,688)	(3,430,099)
Result of exchange rate fluctuations	(445,045)	(633,242)	856,501	1,218,691
Transaction costs	-	-	5,705	8,117
At the end of reporting year	<b>20,079,859</b>	<b>28,571,065</b>	<b>13,684,705</b>	<b>19,471,581</b>

On 30 April 2004 the Company signed long-term loan agreement with AS Hansabanka and AS SEB Latvijas Unibanka for USD 12,500,000, which represents Ls 6,912,500 (10,553,435 EUR), translated at the exchange rate set by the Bank of Latvia as at 30 April 2004, and Ls 6,800,000 (10,381,679 EUR) respectively. Interest rate constitutes 6 months LIBOR plus 1.6% for the part of the loan in USD and 3 months RIGIBOR plus 1.6% for the part of the loan in lats. As at 31 December 2006 the Company's liability to AS Hansabanka for received loan is USD 7,062,500, which represents Ls 3,785,500 (5,386,281 EUR), translated at the exchange rate set by the Bank of Latvia as at 31 December 2006. The Company's loan liability to AS SEB Latvijas Unibanka is Ls 3,485,400 (4,959,277 EUR).

On 21 September 2005 the Company signed a loan agreement with AS Hansabanka for USD 25,000,000. As at 31 December 2005 the loan was not utilized. On 18 April 2006 the Company signed amendments to the agreement on change of the loan currency from USD to EUR. As at 31 December 2006 the Company's liability for the loan to AS Hansabanka amounted to EUR 12,450,949, translated at the exchange rate set by the Bank of Latvia as at 31 December 2006 Ls 8,750,576.

On 30 April 2004 the Company signed credit line agreement with AS Hansabanka and AS SEB Latvijas Unibanka for Ls 2,675,000 (5,610,687 EUR) and Ls 2,800,000 (4,274,809 EUR) respectively. Interest rate was 3 months RIGIBOR plus 1.6%. On 20 May 2005 the Company signed amendments to the credit line agreement with AS Hansabanka and AS SEB Latvijas Unibanka increasing the available amounts of the credit line to Ls 4,058,000 (5,77,014 EUR) and Ls 4,025,000 (5,727,059 EUR) respectively. Fixed interest rate part was decreased to 0.95%. The credit line is repayable in one year. The undrawn credit line as at 31 December 2006 was Ls 4,024,617 (5,726,514 EUR) (31.12.2005: Ls 2,483,353 (3,533,493 EUR)).



**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**10 BORROWINGS (continued)**

The effective interest rates at the balance sheet date were as follows:

	<b>31.12.2006</b>	<b>31.12.2005</b>
Borrowings	4.461% - 6.989%	4.272% - 6%
Credit line	6.556%	4.983%

The exposure of the total principal amount of borrowings to interest rate changes and the periods in which the borrowings reprice are as follows:

	<b>31.12.2006 Ls</b>	<b>31.12.2006 EUR</b>	<b>31.12.2005 Ls</b>	<b>31.12.2005 EUR</b>
6 months or less	20,079,859	28,571,065	13,344,705	18,987,805
6 – 12 months	-	-	340,000	483,776
	<u><b>20,079,859</b></u>	<u><b>28,571,065</b></u>	<u><b>13,684,705</b></u>	<u><b>19,471,581</b></u>

Maturity of the total borrowings is as follows:

Payable in 1 year	7,097,336	10,098,599	4,752,897	6,762,763
Payable between 2 and 5 years	12,982,523	18,472,466	8,931,808	12,708,818
	<u><b>20,079,859</b></u>	<u><b>28,571,065</b></u>	<u><b>13,684,705</b></u>	<u><b>19,471,581</b></u>

The loans are secured by the mortgage of (i) all real estate owned by AS Latvijas balzams and (ii) commercial pledge of all Company's assets on the date of pledging and all assets that might be acquired in the future, and (iii) all shares owned by the Company's largest shareholder, S.P.I. Distilleries B.V., and any other shares that S.P.I. Distilleries B.V. may acquire in the future. Carrying value of the pledged assets of the Company as at 31 December 2006 is Ls 69,192,979 (98,452,739 EUR) (31 December 2005: Ls 53,137,219 (75,607,451 EUR)).

**11 OTHER PAYABLES**

Excise tax	7,557,928	10,753,963	7,456,713	10,609,947
Value added tax	910,883	1,296,070	1,210,201	1,721,961
Social insurance	112,461	160,018	110,374	157,048
Personal income tax	101,780	144,820	81,411	115,837
Natural resources tax	49,762	70,805	48,456	68,947
Real estate tax	92	131	27,649	39,341
Salaries	239,732	341,107	193,979	276,007
Prior years' unpaid dividends	5,235	7,448	5,235	7,449
Accruals for unused annual leave	310,333	441,564	284,219	404,407
Other accrued liabilities	579,474	824,517	472,000	671,595
Other creditors	113,412	161,371	2,375	3,379
	<u><b>9,981,092</b></u>	<u><b>14,201,814</b></u>	<u><b>9,892,612</b></u>	<u><b>14,075,918</b></u>

**12 SEGMENT INFORMATION**

**(a) Primary reporting format – business segments**

The only operational activity of the Company is production of alcoholic drinks. At present AS Latvijas balzams produces more than 120 different types of drinks. Substantially all the Company's production is alcoholic drinks, and therefore the Company has only one reportable business segment. The primary statements and notes presented in these financial statements represent the primary format of segment reporting.

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**12 SEGMENT INFORMATION** (continued)

**(b) Secondary reporting format – geographical segments**

The Company operates in Latvia and it sells drinks in the local market, as well as in foreign markets.

The operations of the Company can be divided into three major segments, which are sales in Latvia, sales to overseas markets through S.P.I group companies and unallocated sales, which mainly represent export sales to unrelated parties. The distribution of the revenues between these segments is as follows:

	<b>2006 Ls</b>	<b>2006 EUR</b>	<b>2005 Ls</b>	<b>2005 EUR</b>
Latvia	27,477,574	39,097,065	26,181,491	37,252,905
Overseas markets through S.P.I group companies	29,156,954	41,486,608	20,152,461	28,674,369
Other export sales	2,308,555	3,284,778	4,813,395	6,848,844
	<b><u>58,943,083</u></b>	<b><u>83,868,451</u></b>	<b><u>51,147,347</u></b>	<b><u>72,776,118</u></b>

The Company is located in Latvia and capital expenditure is incurred only in Latvia.

**13 REVENUE**

Local sales	27,477,574	39,097,065	26,181,491	37,252,905
Export sales	31,439,632	44,734,566	24,953,419	35,505,517
Other sales (spirit, raw materials)	25,877	36,820	12,437	17,696
	<b><u>58,943,083</u></b>	<b><u>83,868,451</u></b>	<b><u>51,147,347</u></b>	<b><u>72,776,118</u></b>

**14 COST OF SALES**

Variable costs	43,860,747	62,408,221	37,504,962	53,364,753
<i>Materials</i>	38,097,402	54,207,719	33,869,177	48,191,497
<i>Goods purchased</i>	336,683	479,057	383,262	545,333
<i>Salary expenses</i>	1,895,106	2,696,493	1,499,486	2,133,576
<i>Social insurance</i>	455,190	647,677	360,394	512,794
<i>Electricity</i>	448,279	637,844	364,715	518,943
<i>Natural resources tax</i>	517,307	736,062	532,056	757,047
<i>Impairment of receivables and inventory, and other accruals</i>	224,444	319,355	251,090	357,269
<i>Other expenses</i>	1,886,336	2,684,014	244,782	348,294
Fixed costs	3,903,413	5,554,056	3,555,195	5,058,587
<i>Depreciation and amortisation</i>	1,403,266	1,996,668	1,421,600	2,022,755
<i>Salary expenses</i>	884,778	1,258,926	731,050	1,040,190
<i>Social insurance</i>	209,798	298,516	173,215	246,463
<i>Repair expenses</i>	971,129	1,381,792	840,819	1,196,378
<i>Insurance</i>	62,644	89,134	61,806	87,942
<i>Laboratory expenses</i>	54,453	77,480	34,806	49,524
<i>Other expenses</i>	317,345	451,540	291,899	415,335
	<b><u>47,764,160</u></b>	<b><u>67,962,277</u></b>	<b><u>41,060,157</u></b>	<b><u>58,423,340</u></b>

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**15 SELLING EXPENSES**

	<b>2006</b>	<b>2006</b>	<b>2005</b>	<b>2005</b>
	<b>Ls</b>	<b>EUR</b>	<b>Ls</b>	<b>EUR</b>
Salary expenses	1,097,370	1,561,417	830,481	1,181,668
Social insurance	262,073	372,896	199,588	283,988
Depreciation and amortisation	242,513	345,065	145,848	207,523
Advertising	1,997,017	2,841,499	1,706,470	2,428,088
Transportation cost	899,587	1,279,997	665,557	947,002
Warehouse maintenance	80,494	114,533	55,970	79,638
Other expenses	335,951	478,015	238,882	339,899
	<b><u>4,915,005</u></b>	<b><u>6,993,422</u></b>	<b><u>3,842,796</u></b>	<b><u>5,467,806</u></b>

**16 ADMINISTRATIVE EXPENSES**

Salary expenses	990,038	1,408,697	798,332	1,135,924
Social insurance	161,609	229,949	145,143	206,520
Communication and postal expenses	243,848	346,964	212,655	302,581
Office expenses	108,629	154,565	93,166	132,563
Professional fees	168,935	240,373	191,593	272,612
IT maintenance	264,088	375,763	297,202	422,880
Representations	213,932	304,398	89,856	127,854
Security	165,389	235,327	198,859	282,951
Management services	1,060,479	1,508,926	1,026,654	1,460,797
Transportation	127,453	181,349	105,345	149,892
Business trip	73,504	104,587	82,990	118,084
Personnel education and training	10,687	15,206	10,498	14,937
Depreciation	306,080	435,513	242,571	345,147
Real estate tax	175,534	249,762	138,493	197,058
Financial help, sponsorship	135,948	193,437	101,906	144,999
Healthcare, health insurance	68,785	97,872	54,079	76,947
Accruals for unused annual leave	26,114	37,157	68,149	96,967
Trade union, cultural and other expenses	53,956	76,772	201,020	286,026
Other expenses	25,832	36,756	27,256	38,784
Accruals for premiums	194,332	276,510	-	-
	<b><u>4,575,172</u></b>	<b><u>6,509,883</u></b>	<b><u>4,085,767</u></b>	<b><u>5,813,523</u></b>

**17 OTHER INCOME**

Proceeds from sale of inventory	18,573	26,427	32,578	46,354
Proceeds from sale of materials	120,121	170,917	74,317	105,744
Sales of brand names	-	-	1,155,000	1,643,417
Services rendered	467,514	665,212	308,423	438,846
Difference from purchase of certificates	-	-	10,089	14,355
Net gain on disposal of property, plant and equipment (see Note 27b)	1,118,710	1,591,781	-	-
Other income	479,182	681,815	139,577	198,601
	<b><u>2,204,100</u></b>	<b><u>3,136,152</u></b>	<b><u>1,719,984</u></b>	<b><u>2,447,317</u></b>

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**18 OTHER EXPENSES**

	<b>2006</b> <b>Ls</b>	<b>2006</b> <b>EUR</b>	<b>2005</b> <b>Ls</b>	<b>2005</b> <b>EUR</b>
Net loss on disposal of property, plant and equipment	-	-	99,083	140,982
Fines and penalties	15,219	21,655	3,512	4,997
Loss on revaluation of property, plant and equipment	-	-	117,428	167,085
Other expenses	60,301	85,800	159,118	226,405
	<b>75,520</b>	<b>107,455</b>	<b>379,141</b>	<b>539,469</b>

**19 EXPENSES BY NATURE**

Materials	38,097,402	54,207,719	33,869,177	48,191,497
Employee benefit expenses	5,955,962	8,474,570	4,737,689	6,741,124
Depreciation and amortisation	1,951,859	2,777,245	1,810,019	2,575,425
Advertising	1,997,017	2,841,499	1,706,470	2,428,088
Management services	1,060,479	1,508,926	1,026,654	1,460,797
Repair expenses	971,129	1,381,792	840,819	1,196,378
Net increase of provisions	224,444	319,355	251,090	357,269
Transportation costs	899,587	1,279,997	665,557	947,002
Natural resource tax	517,307	736,062	532,056	757,047
IT maintenance	264,088	375,763	297,202	422,880
Real estate tax	175,534	249,762	138,493	197,058
Other expenses	5,215,049	7,420,346	3,492,635	4,969,572
	<b>57,329,857</b>	<b>81,573,036</b>	<b>49,367,861</b>	<b>70,244,137</b>

**20 FINANCE INCOME / COSTS**

Interest income	501,613	713,731	6,829	9,717
Income from penalties	72,471	103,117	137,846	196,137
<b>Finance income</b>	<b>574,084</b>	<b>816,848</b>	<b>144,675</b>	<b>205,854</b>
Interest on long-term loans	(847,271)	(1,205,558)	(551,010)	(784,017)
Interest on credit line	(228,964)	(325,786)	-	-
Net loss from exchange rate fluctuations	(150,373)	(213,962)	(103,115)	(146,719)
<b>Finance costs</b>	<b>(1,226,608)</b>	<b>(1,745,306)</b>	<b>(654,125)</b>	<b>(930,736)</b>

**21 INCOME TAX EXPENSE**

**(a) Components of income tax**

Deferred income tax	(120,472)	(171,416)	(8,996)	(12,800)
Current income tax	706,455	1,005,195	621,340	884,087
	<b>585,983</b>	<b>833,779</b>	<b>612,344</b>	<b>871,287</b>

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**21 INCOME TAX EXPENSE** (continued)

**(b) Reconciliation of accounting profit to tax charges**

Corporate income tax differs from the theoretically calculated tax amount that would arise applying the 15% rate stipulated by the law to profit before taxation:

	31.12.2006 Ls	31.12.2006 EUR	31.12.2005 Ls	31.12.2005 EUR
<b>Profit before income tax</b>	<b>3,164,802</b>	<b>4,503,108</b>	<b>2,990,020</b>	<b>4,254,415</b>
Theoretically calculated tax at a tax rate of 15%	474,720	675,466	448,503	638,162
Expenses not deductible for tax purposes	164,969	234,730	223,681	318,269
Non-taxable income	-	-	(510)	(725)
Tax discount for donations	(53,706)	(76,417)	(59,877)	(85,197)
Adjustment for deviations from statutory accounts	-	-	547	778
<b>Tax charge</b>	<b>585,983</b>	<b>833,779</b>	<b>612,344</b>	<b>871,287</b>

**(c) Deferred income tax liability**

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. The offset amounts are as follows:

Deferred tax assets:				
- Deferred tax asset to be recovered within 12 months	(122,300)	(174,017)	(8,448)	(12,020)
	(122,300)	(174,017)	(8,448)	(12,020)
Deferred tax liabilities:				
- Deferred tax liability to be settled within 12 months	1,281,430	1,823,312	-	-
- Deferred tax liability to be settled after more than 12 months	1,266,892	1,802,624	1,344,478	1,913,020
	2,548,322	3,625,936	1,344,478	1,913,020
<b>Net deferred income tax liability</b>	<b>2,426,022</b>	<b>3,451,919</b>	<b>1,336,030</b>	<b>1,901,000</b>

The movement on the deferred income tax account is as follows:

	2006 Ls	2006 EUR	2005 Ls	2005 EUR
Beginning of the year	1,336,030	1,900,999	577,421	821,596
Deferred tax charged to revaluation reserve	1,210,464	1,722,335	767,605	1,092,204
Income statement charge	(120,472)	(171,416)	(8,996)	(12,800)
<b>End of the year</b>	<b>2,426,022</b>	<b>3,451,918</b>	<b>1,336,030</b>	<b>1,901,000</b>

The movement of deferred tax assets and liabilities during the year, without taking into consideration the offsetting of balances within the same tax jurisdiction, is as follows:

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**21 INCOME TAX EXPENSE (continued)**

**(c) Deferred income tax liability (continued)**

	Property, plant and equipment Ls	Accruals for unused annual leave Ls	Accruals for bonuses Ls	Provisions for slow moving stock Ls	Total Ls
<b>At 1 January 2005</b>	<b>676,262</b>	<b>(32,411)</b>	<b>(2,250)</b>	<b>(64,180)</b>	<b>577,421</b>
Charged / (credited) to income statement	(3,286)	(10,222)	2,198	2,314	(8,996)
Charged to equity	767,605	-	-	-	767,605
<b>At 31 December 2005</b>	<b>1,440,581</b>	<b>(42,633)</b>	<b>(52)</b>	<b>(61,866)</b>	<b>1,336,030</b>
Charged / (credited) to income statement	(102,723)	(3,917)	52	(13,884)	(120,472)
Charged to equity	1,210,464	-	-	-	1,210,464
<b>At 31 December 2006</b>	<b>2,548,322</b>	<b>(46,550)</b>	<b>-</b>	<b>(75,750)</b>	<b>2,426,022</b>

	EUR	EUR	EUR	EUR	EUR
<b>At 1 January 2005</b>	<b>962,234</b>	<b>(46,117)</b>	<b>(3,201)</b>	<b>(91,320)</b>	<b>821,596</b>
Charged / (credited) to income statement	(4,676)	(14,544)	3,127	3,293	(12,800)
Charged to equity	1,092,204	-	-	-	1,092,204
<b>At 31 December 2005</b>	<b>2,049,762</b>	<b>(60,661)</b>	<b>(74)</b>	<b>(88,027)</b>	<b>1,901,000</b>
Charged / (credited) to income statement	(146,161)	(5,574)	74	(19,755)	(171,416)
Charged to equity	1,722,335	-	-	-	1,722,335
<b>At 31 December 2006</b>	<b>3,625,936</b>	<b>(66,235)</b>	<b>-</b>	<b>(107,782)</b>	<b>3,415,919</b>

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**22 EARNINGS PER SHARE (EXPRESSED IN SANTIMS OR EURO CENTS PER SHARE)**

The Company has no dilutive potential shares therefore diluted earnings per share are equal to basic earning per share.

Earnings per share are calculated by dividing the profit for the reporting year with the average number of shares in issue during the reporting year.

	<b>2006 Ls</b>	<b>2006 EUR</b>	<b>2005 Ls</b>	<b>2005 EUR</b>
Profit attributable to equity holders of the Company	2,578,819	3,669,329	2,377,676	3,383,128
Weighted average number of shares in issue during the reporting year	<u>7,496,900</u>	<u>7,496,900</u>	<u>7,496,900</u>	<u>7,496,900</u>
Earnings per share (in santims and euro cents)	<u><b>34.40</b></u>	<u><b>48.94</b></u>	<u><b>31.72</b></u>	<u><b>45.13</b></u>

**23 CASH GENERATED FROM OPERATIONS**

	<b>2006 Ls</b>	<b>2006 EUR</b>	<b>2005 Ls</b>	<b>2005 EUR</b>
Profit before corporate income tax	3,164,802	4,503,108	2,990,020	4,254,415
<u>Adjustments for:</u>				
- depreciation and amortization (Notes 3 and 4)	1,951,859	2,777,245	1,810,019	2,575,425
- increase / (decrease) of provisions for impairment of inventory	92,558	131,698	221,573	315,270
- loss / (gain) on foreign currency exchange rate fluctuation	(356,416)	(507,134)	856,501	1,218,691
- interest expenses (Note 20)	1,076,235	1,531,344	551,010	784,017
- interest income (Note 20)	(501,613)	(713,731)	(6,829)	(9,717)
- loss / (gain) from disposal of property, plant and equipment and revaluation	(1,118,710)	(1,591,781)	217,339	309,246
- write off of borrowing costs	-	-	5,705	8,117
<u>Change in working capital</u>				
- debtors	(260,657)	(370,880)	(4,035,652)	(5,742,215)
- inventory	(2,430,635)	(3,458,482)	(1,449,026)	(2,061,778)
- creditors	821,299	1,168,603	5,665,727	8,061,602
	<u><b>2,438,722</b></u>	<u><b>3,469,990</b></u>	<u><b>6,826,387</b></u>	<u><b>9,713,073</b></u>

**24 AVERAGE NUMBER OF EMPLOYEES**

	<b>2006</b>	<b>2005</b>
Average number of employees during the reporting year:	<u><b>779</b></u>	<u><b>726</b></u>

**AS LATVIJAS BALZAMS**  
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**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**25 PERSONNEL EXPENSES**

	2006 Ls	2006 EUR	2005 Ls	2005 EUR
Salaries and social insurance for production staff	3,444,872	4,901,611	2,764,146	3,933,026
Salaries and social insurance for distribution staff	1,359,443	1,934,313	1,030,069	1,465,656
Salaries and social insurance for administration staff	1,151,646	1,638,645	943,475	1,342,444
<b>Total*</b>	<b><u>5,955,961</u></b>	<b><u>8,474,569</u></b>	<b><u>4,737,690</u></b>	<b><u>6,741,126</u></b>
including:				
the Board members' and management remuneration				
- salary expenses	568,215	808,497	437,124	621,971
- social insurance	61,137	86,990	55,000	78,258

According to the shareholders' decision, the Board and the Council members do not receive additional remuneration for fulfilment of their duties.

\* Includes social insurance of Ls 1,088,670 (1,549,038 EUR) (2005 – Ls 878,340 (1,249,765 EUR)).

In accordance with the rulings of the Cabinet of Ministers of Latvia 74% (2005: 75%) of the social insurance costs are used to fund the state defined contribution pension system.

During the reporting year, no loans were issued to members of the Council, the Board and the Management staff.

**26 ISSUED GUARANTEES AND PLEDGES**

On 26 January 2006 the Company issued guarantee to AS Parex bank regarding creditline of SIA Bravo in amount of EUR 4,268,615 (Ls 3,000,000) for the purchase of 100% of UAB Darija shares. The repayment term for this credit line is 25 January 2008.

On 18 April 2006 agreement No. KD05392/2 was concluded between AS SEB Latvijas Unibanka and the Company regarding AS Latvijas balzams as security for the financial liabilities of S.P.I. Spirits (Cyprus) against the bank in amount of USD 10,000,000 (as at 31.12.2006: Ls 5,360,000 (7,626,593 EUR)). Guarantee is issued for the period until 16 April 2008.

The Company issued guarantee to AS Parex bank regarding SPI Spirits (UK) Limited liabilities relating to issuance of VISA, Eurocard/MasterCard, Maestro, VISA Electron and opening of bank account with a limit of USD 100,000 (as at 31.12.2006: Ls 53,600 (76,266 EUR)).

**27 TRANSACTIONS WITH RELATED PARTIES**

The parent company of the Company, who owns 88.05% of shares of the Company, is S.P.I. Distilleries B.V., which is registered in Netherlands. The ultimate parent company is S.P.I. Group SA, which is registered in Switzerland and its majority shareholder is Mr. Shefler.

During year 2006 the Company had purchase and sale transactions with the following related companies which are direct or indirect subsidiaries of SPI Group SA: S.P.I. Spirits Ltd. (Cyprus), Spirits Product International IP B.V. (Netherlands), Tambovskoje spirtovodocnoje predpriyatije Talvis OAO (Russia), S.P.I. Worldwide Trade Ltd. (Netherlands), Torgovi Dom Rosvestalko (Russia), S.P.I. Production B.V. (Netherlands), S.P.I. Resources B.V (Netherlands), UAB Baltijos alkoholiniai produktai (Lithuania), SPI-RVVC OAO (Russia), SIA Bravo (Latvia), UAB Darija (Lithuania), UAB Bennet Distributors (Lithuania),



**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**27 TRANSACTIONS WITH RELATED PARTIES** (continued)

SIA Vertikālā pasaule (Latvia), SIA Meirovica 35 (Latvia) and Mr. Shefler.

**(a) sale of goods**

	<b>2006 Ls</b>	<b>2006 EUR</b>	<b>2005 Ls</b>	<b>2005 Ls</b>
S.P.I. Spirits Ltd.	25,609,163	36,438,556	20,167,165	28,695,291
Torgovi Dom Rosvestalko	-	-	966,002	1,374,497
Torgovy dom SPI-TRADE	-	-	4,336	6,170
SPI-RVVC OAO	151,316	215,303	16,145	22,972
SIA Bravo	106,254	151,186	65,693	93,473
UAB Bennet Distributors	3,217,343	4,577,867	-	-
S.P.I Worldwide Trade Ltd.	-	-	70,280	99,999
	<b>29,084,076</b>	<b>41,382,912</b>	<b>21,289,621</b>	<b>30,292,402</b>

**(b) sale of assets**

Mr. Shefler (net cash received)*	4,622,432	6,577,128	-	-
SIA Meierovica 35	1,564,001	2,225,373	-	-
	<b>6,186,433</b>	<b>8,802,501</b>	<b>-</b>	<b>-</b>

Sale of property, plant and equipment to Mr. Shefler was performed by contributing those assets in share capital of SIA Meierovica 35 and subsequent sale of all shares of SIA Meierovica 35 to Mr. Shefler. Gain on this transaction is included in net gain on disposal of property, plant and equipment (Note 17).

**(c) services rendered (including interest on loans issued)**

UAB Bennet Distributors	504	717	-	-
S.P.I. Spirits Ltd.	334,726	476,272	241,901	344,194
SIA Bravo	6,065	8,630	5,619	7,995
Spirits Product International IP B.V.	1,016	1,446	1,859	2,645
Spirits International N.V.	-	-	1,155,949	1,644,767
UAB Baltijos alkoholiniai produktai	2,510	3,571	2,117	3,013
SIA Meierovica 35	81,488	115,947	-	-
SIA Vertikala pasaule	4,795	6,823	-	-
SPI Production B.V.	454,876	647,230	-	-
SPI Resources B.V.	81,234	115,586	-	-
	<b>967,214</b>	<b>1,376,222</b>	<b>1,407,445</b>	<b>2,002,614</b>

**(d) purchase of goods**

SPI-RVVC OAO	6,213,290	8,840,715	5,292,055	7,529,916
S.P.I. Spirits Ltd.	23,297	33,149	77,206	109,854
Spirits International GmbH	-	-	10,366	14,750
CJSC Sojuzplodimport	-	-	56,491	80,379
Tambovskoje spirtovodocnoje predpriyatije Talvis OAO	2,708,033	3,853,184	1,500,999	2,135,729
UAB Darija	3,063	4,358	-	-
UAB Bennet Distributors	50,909	72,437	-	-
SIA Bravo	1,358	1,932	18,705	26,615
	<b>8,999,950</b>	<b>12,805,775</b>	<b>6,955,822</b>	<b>9,897,243</b>

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**27 TRANSACTIONS WITH RELATED PARTIES** (continued)

**(e) services received**

	<b>31.12.2006</b>	<b>31.12.2006</b>	<b>31.12.2005</b>	<b>31.12.2005</b>
	<b>Ls</b>	<b>EUR</b>	<b>Ls</b>	<b>EUR</b>
Tambovskoje spirtovodocnoje predprijetije Talvis OAO	1,954	2,780	-	-
SIA Meierovica 35	42,180	60,017	-	-
UAB Bennet Distributors	119,330	169,792	-	-
SIA Bravo	7,625	10,849	-	-
Spirits Product International IP B.V.	249,647	355,216	387,190	550,922
S.P.I. Spirits Ltd.	1,103,625	1,570,317	806,597	1,147,684
UAB Baltijos alkoholiniai produktai	2,671	3,800	25,500	36,283
	<b>1,527,032</b>	<b>2,172,771</b>	<b>1,219,287</b>	<b>1,734,889</b>

**(f) accounts payable to related parties**

Spirits International N.V.	263,542	374,986	-	-
SIA Meierovica 35	8,295	11,803	-	-
Torgovi Dom SPI-Trade	29	41	-	-
UAB Bennet Distributors	1,796	2,555	-	-
SPI-RVVC OAO	-	-	58,024	82,560
SIA Bravo	7,664	10,905	16,848	23,973
Spirits Product International IP B.V.	249,648	355,217	283,580	403,498
S.P.I. Spirits Ltd.	946,062	1,346,125	177,545	252,624
Tambovskoje spirtovodocnoje predprijetije Talvis OAO	6,679	9,504	-	-
	<b>1,483,715</b>	<b>2,111,136</b>	<b>535,997</b>	<b>762,655</b>

Payables are payable in cash and are not secured by a pledge or otherwise.

**(g) accounts receivable from related parties**

S.P.I. Spirits Ltd.	3,889,817	5,534,711	4,561,410	6,490,302
Torgovi Dom Rosvestalko	-	-	383,972	546,343
Spirits Product International IP B.V.	11,525	16,399	10,808	15,379
SIA Bravo	48,566	69,103	36,988	52,629
CJCS Sojuzplodimport	-	-	3,239	4,609
UAB Bennet Distributors	1,430,001	2,034,708	-	-
S.P.I. Production B.V.	58,109	82,682	-	-
SPI-RVVC OAO	198,740	282,782	1,129	1,606
SPI Resources B.V.	2,786	3,964	-	-
Torgovy dom SPI-TRADE	-	-	5,485	7,804
Spirits International N.V.	-	-	1,054	1,500
SIA Vertikala pasaule	1,244	1,770	-	-
SIA Meierovica 35*	1,930,744	2,747,201	-	-
UAB Baltijos Alkoholiniai Produktai	4,628	6,585	2,118	3,014
S.P.I Worldwide Trade Ltd.	70,280	99,999	70,280	99,999
	<b>7,646,440</b>	<b>10,879,904</b>	<b>5,076,483</b>	<b>7,223,185</b>

There are no significant bad and doubtful debts due from related parties in 2005 and 2006.

\* interest of 3 months RIGIBOR + 0.95% times 1.05 on loan to SIA Meirovica 35 is charged. Effective interest rate as at 31 December 2006 was 5.43%. The rest of the receivables are interest free.

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**27 TRANSACTIONS WITH RELATED PARTIES** (continued)

**(h) loans to related parties**

	<b>31.12.2006</b>	<b>31.12.2006</b>	<b>31.12.2005</b>	<b>31.12.2005</b>
	<b>Ls</b>	<b>EUR</b>	<b>Ls</b>	<b>EUR</b>
S.P.I. Production B.V.*	14,477,762	20,600,000	-	-
S.P.I. Spirits Ltd.	-	-	2,965,000	4,218,814
SIA Vertikāla pasaule**	35,000	49,800	-	-
UAB Baltijos Alkoholiniai Produktai***	66,063	94,000	66,063	94,000
	<b>14,578,825</b>	<b>20,743,800</b>	<b>3,031,063</b>	<b>4,312,814</b>

	<b>2006</b>	<b>2006</b>	<b>2005</b>	<b>2005</b>
	<b>Ls</b>	<b>EUR</b>	<b>Ls</b>	<b>EUR</b>
At the beginning of reporting year	3,031,063	4,312,814	-	-
Loans issued during the year	18,728,371	26,648,071	3,031,063	4,312,814
Loans repaid during the year	(7,080,583)	(10,074,762)	-	-
Result of exchange rate fluctuations	(100,026)	(142,324)	-	-
At the end of reporting year	<b>14,578,825</b>	<b>20,743,799</b>	<b>3,031,063</b>	<b>4,312,814</b>
Including:				
- short-term loans	101,063	143,800	3,031,063	4,312,814
- long-term loans – receivable between 2 to 5 years	14,477,762	20,600,000	-	-
	<b>14,578,825</b>	<b>20,743,800</b>	<b>3,031,063</b>	<b>4,312,814</b>

\* On 20 April 2006 the Company concluded a long-term loan agreement with S.P.I. Production B.V. in amount of EUR 20,600,000, translated at the exchange rate set by the Bank of Latvia as at 31 December 2006 Ls 14,477,762. The maturity term is 20 July 2010 or according to bilateral agreement 20 July 2015. The applied interest rate consists of 1.4% per annum fixed part + 3 months EURIBOR variable part. The effective interest rate in 2006 has been 4.1%.

\*\* On 20 April 2006 the Company concluded a loan agreement with SIA Vertikālā pasaule in amount of Ls 100,000 (142,287 EUR) with a fixed interest rate of 5% per annum. The maturity term of the loan is 30 June 2007. As at 31 December 2006 the total outstanding loan balance is Ls 35,000 (49,800 EUR).

\*\*\* On 3 December 2005 the Company signed a loan agreement with UAB Baltijos Alkoholiniai Produktai for loan in amount of EUR 107,000 with fixed interest rate of 4.5% per annum. The maturity term is 31 December 2006. Until 31 December 2006 the Company issued EUR 94,000 which represents Ls 66,063, translated at the official exchange rate set by the Bank of Latvia as at 31 December 2006. Loan is not reimbursed. In 2006 the loan liability was transferred to UAB Bennet Distributors (Lithuania).

Loans are payable in cash and are not secured by a pledge or otherwise.

**(i) royalty payments**

The Company is leasing trade marks from S.P.I. group. The amount of the royalties depends on the amount of the produced drinks subject to royalty payments. Royalty payments are included in total services received (Note 27(e)). According to the management estimates the royalty payments during 2007 will be approximately Ls 400 (569 EUR) thousand (31.12.2005: Ls 739 (1,052 EUR) thousand).

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**28 FINANCIAL RISK MANAGEMENT**

The Company's activities expose it to a variety of financial risks: market risk (including currency risk, cash flow interest rate risk), credit risk and liquidity risk. The management of the Company seeks to minimize potential adverse effects on the Company's financial performance.

**(a) Credit risk**

Financial assets which potentially subject the Company to concentration of credit risk consist principally of cash, trade receivables and issued loans. The Company has policies in place to ensure that sales of products and services are made to customers with an appropriate credit history. Customer debts are reported at their recoverable value. The partners of the Company in money transactions are local and foreign financial institutions with adequate credit history. Of the total sales 49% are made to related parties (2005: 42%) and 46% are made to a single unrelated customer (2005: 51%). The credit risk concentration arising from transactions with related parties is disclosed in Notes 27(g) and 27(h). The receivable from the largest unrelated debtor represents 88% (31 December 2005: 84%) of the total trade receivables from unrelated parties.

**(b) Foreign exchange risk**

The Company is exposed to foreign exchange risk arising from various currency exposures primarily because the majority of raw materials are purchased in EUR and USD, but a significant part of goods are sold in local market and exported to the markets dominated by Euro and US dollar. As of 1 January 2005 the Lats exchange rate has been tied to EUR, therefore the LVL/EUR exchange rate fluctuation possibilities are limited, and any substantial influence of this exchange rate on future financial results is not foreseen. In order to decrease influence of US dollar over the operations of the Company, part of the financing received from credit institutions is denominated in US dollars.

**(c) Interest rate risk**

The Company is exposed to changes in interest rates, as largest portion of liabilities is interest bearing liabilities having floating interest rates (Note 10) and the Company's interest bearing assets have floating interest rates (Note 27 (h)). The Company continues to monitor the market in general, but at present do not consider it cost efficient to enter into any long-term interest rate swaps to limit the risk of increase in interest cost.

**(d) Liquidity risk**

The Company pursues a prudent liquidity risk management maintaining sufficient credit resources that allow to settle liabilities when they fall due. As at 31 December 2006 the Company's current assets exceeded its current liabilities by Ls 8.7 (12.4 EUR) million (31.12.2005: Ls 11.3 (16.1 EUR) million). The total available credit line amounts to Ls 8,083 (11,501 EUR) thousand. Unutilized portion of credit line as at 31 December 2006 is Ls 4,025 (5,727 EUR) thousand.

**(e) Fair value**

There are no material differences between the carrying amounts of financial assets and liabilities and their fair values. During the year, the Company did not use any derivative financial instruments.

**29 CONTINGENT LIABILITIES**

The Company is not aware of any potential litigations except for the litigation with SIA Aroma Floris's on damages in amount of Ls 37,366 (53,167 EUR). During the time of signing of these financial statements, a protest note has been issued to the director of the Civil case department of Supreme Court of the Republic of Latvia on decisions of the Appeal court and Cassation court.

**AS LATVIJAS BALZAMS**  
**FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2006**

**NOTES TO THE FINANCIAL STATEMENTS** (continued)

**30 TAX CONTINGENT LIABILITIES**

The tax authorities have performed the complex tax audit for the period from 2002 till 2004. The outcome of the audit is not material to these financial statements.

The tax authorities have the right to inspect the accounting records for the last three years and apply additional tax liabilities and penalties. The management of the Company is not aware of any circumstances that could potentially give rise to significant liabilities in the future.

**31 SUBSEQUENT EVENTS**

There are no subsequent events since the last date of the reporting year, which would have a significant effect on the financial position of the Company as at 31 December 2006.