FINANSU UN KAPITĀLA TIRGUS KOMISIJA

ANNUAL REPORT OF THE FINANCIAL AND CAPITAL MARKET COMMISSION FOR 2001

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INTRODUCTION

The Financial and Capital Market Commission (hereinafter – the Commission) commenced its activities on 1 July 2001 thereby becoming the legal successor to the rights, obligations and liabilities of the Insurance Supervision Inspectorate, the Securities Market Commission, administration of the Deposits Guarantee Fund as well as to the rights, obligations and liabilities of the Bank of Latvia in the field of credit institution supervision.

The Commission is an autonomous public institution and the purpose of its activities is to promote the protection of interests of investors, depositors and the insured and the development and stability of the financial and capital market. To this end, the Commission regulates and supervises the financial and capital market and activities of its participants.

The year 2001 saw the development of a strategy for the Commission's activities and a clear definition of steps to be taken to fulfil its functions as prescribed by the Law on the Financial and Capital Market Commission. In 2001, the Commission re-approved 82 regulatory enactments governing activities of financial and capital market participants.

Since the principal aim of Latvia's foreign and economic policies is its integration with the European Union (hereinafter – EU), the Commission proceeds with the harmonisation of regulatory requirements governing the activities of participants in the financial and capital market with the European Community (hereinafter – EC) directives and recommendations.

In 2001, within the framework of the financial sector assessment programme, the World Bank and the International Monetary Fund gave a positive evaluation of the Latvian financial sector, which confirmed the general competitiveness of the Latvian financial market and the quality of the market supervision. Experts of the World Bank and the International Monetary Fund concluded that Latvia was largely compliant with the Basel Committee Core Principles for Effective Banking Supervision. The finding was similar for the insurance sector where supervision was adequate and Latvia was largely observant of the IAIS Core Principles. The Principles of Securities Regulation of IOSCO and the OECD Principles of Corporate Governance were also largely implemented. Latvia exhibited a high degree of transparency in virtually all of the areas in which it had been assessed (banking, insurance, and securities market supervision; and in the spheres of monetary policy and the payment system).

This annual report includes information concerning activities of the supervisory institutions whose functions were taken over by the Commission, as well as the financial and capital market, during the entire year 2001, whereas financial statements of the Commission cover six months, i.e., from its inception on 1 July 2001 until 31 December 2001.

On 22 February 2002, the Council of the Financial and Capital Market Commission passed Resolution No. 58 (Minutes No.7, Paragraph 3) on the Approval of the Annual Report of the Financial and Capital Market Commission for 2001.

COUNCIL OF THE FINANCIAL AND CAPITAL MARKET COMMISSION

Uldis Cērps (middle)
Chairman

Jānis Brazovskis (extreme left)
Deputy Chairman

Jānis Placis (second from right)
Director of the Supervision Department
Gvido Romeiko (extreme right)
Director of the Legal and Licensing Department
Ludmila Vojevoda (second from left)
Director of the Regulations and Statistics Department

"The purpose of activities of the Commission shall be to promote the protection of interests of investors, depositors and the insured as well as the development and stability of the financial and capital market."

(Article 5 of the Law on the Financial and Capital Market Commission)

STRATEGY FOR REGULATION AND SUPERVISION OF THE FINANCIAL AND CAPITAL MARKET

The strategic goals of the Financial and Capital Market Commission are as follows:
- promotion of *stability* of the financial and capital market;
- promotion of *development* of the financial and capital market; and
- *protection* of interests of investors, depositors and the insured.

1. Stability

The principal strategic goal of the Commission is to ensure the overall stability of the financial and capital market. This means that, within the framework of law, the Commission will take measures against participants in the financial and capital market if their actions or failure to act may cause instability of the entire financial and capital market or of its separate sectors. In order to promote stability, the Commission sets forth the following tasks:

1.1. to increase overall confidence in the Latvian financial system. At present, the confidence of Latvian residents in the financial and capital market lags behind the level in the EU Member States. The Commission will act purposefully to increase the confidence of consumers in the financial and capital market and to achieve or even exceed the levels of confidence specific to EU Member States;

1.2. to monitor risks associated with the Latvian financial system. Since the primary objective of the Commission is the stability of the financial and capital market, the Commission will pay a close attention to the monitoring of risks of major market participants;

1.3. to reduce possible losses. One of the tasks of the Commission is to see to it that market participants are able to meet their obligations. The solvency of market participants is determined by economic and other factors. The supervisory council, management board and major shareholders of each market participant are responsible for the financial stability and operations of the company they own or manage. Likewise, clients competent in financial matters such as large companies and institutional investors must assume full responsibility for their actions. In order to minimise the likelihood of insolvency of market participants, the Commission will supervise the compliance with the minimum capital adequacy requirements, monitor activities of market participants and establish appropriate methods for the evaluation of the financial standing of market participants. The activities of the Commission are directed at the reduction of the effect of possible insolvency of individual financial and capital market participants on the overall confidence of clients in the Latvian financial system;

1.4. to reduce the possibility of using the Latvian financial system to launder proceeds derived from criminal activity. The Commission will act purposefully to maintain and augment the reputation of the Latvian financial system. The Commission will improve and develop the procedures regarding supervision and control of financial and capital market participants in compliance with the requirements of EC directives and best supervisory practices. The Commission will oversee the internal control procedures of financial and capital market participants in order to prevent any possibility of using the Latvian financial system to launder proceeds derived from criminal activity;

1.5. security of information technology. Taking into account the increasing role of information technologies in the provision of financial services, the Commission will see to it that market participants comply with the security rules established for information systems. The Commission will adjust these rules taking into account the degree of risk caused by the information technologies used by market participants. When performing an analysis of market participants, the Commission staff will regularly check the compliance with said rules; and

1.6. efficiency of the Commission expenditure. Being aware of the necessity to ensure qualitative supervision of the financial and capital market, the Commission will take into account interests of financial and capital market participants in order to efficiently utilise financial resources. Simultaneously, the Commission will avoid incurring expenses that fail to conform to its objectives.

2. Development

In order to promote development, the Commission sets forth the following tasks:

2.1. to ensure free competition in the financial and capital market. Fair and open competition provides consumers with increased ability to choose among market products and prices. The Commission will use all legal regulatory measures and resources at its disposal to penalize those market participants that resort to unfair means of competition, including those unjustifiable from either an economic or ethical point of view. Methods incompatible with fundamental market principles will not be applied in order to artificially reduce the number of market participants. Moreover, market stability also implies that market participants remain competitive in Latvia as well as internationally;

2.2. to promote innovation. The Commission will not restrict licensing of new market participants without good reason. New participants must be financially strong and professional, maintain impeccable reputation and be in compliance with the requirements of laws, EC directives and good practices. The Commission will not restrict the expansion of activities of the present market participants. Within the scope of its competence, the Commission will promote the introduction of new financial services, products and technologies that, in turn, will increase the competitiveness of market participants;

2.3. to analyse and improve the taxation system. The Commission will actively participate in the analysis and improvement of the system of taxes and duties applicable to financial and capital market participants with a view of promoting a system of taxation that would be favourable to the development of the financial market at large and the capital market in particular. The Commission will consistently harmonise regulatory requirements governing the activities of financial and capital market participants with the requirements of the relevant EC directives and recommendations of international financial and capital market supervisory organisations;

2.4. to implement the international accounting standards. The EU advances towards a universal application of international accounting standards (hereinafter - IAS) to financial statements of financial and capital market participants, including companies listed on the stock exchange. Since credit institutions, which are the major Latvian financial market participants, are already now preparing their financial statements in accordance with IAS, the Commission will introduce mandatory requirements for drawing up financial statements in accordance with IAS to all other market participants; and

2.5. to co-operate with professional associations of market participants. Within the framework of dialogue, the Commission will effectively co-operate with professional associations set up by market participants, including the Consultative Council of the Financial and Capital Market Commission, in order to promote initiatives important for the financial market development.

3. Protection of Interests of Investors, Depositors and the Insured

In order to protect the interests of investors, depositors and the insured, the Commission sets forth the following tasks:

3.1. transparency of the Commission's budget. The annual budget of the Commission will be available to the public both on its Internet home page and at its offices. When drawing up the budget, the Commission will take into account opinions of public organisations and professional associations of market participants, investors and the insured. The information on assets of the guarantee funds, investors, and the insured will be made available on an ongoing basis;

3.2. transparency of the Commission's regulations and ordinances. The regulatory requirements and ordinances issued by the Commission, financial and capital market statistics, and the Commission's strategy will be published on the Internet and made available on the premises of the Office of the Commission;

3.3. availability of information regarding market participants to the general public. The Commission will see to it that the financial and capital market participants publish information regarding their financial situation, performance results and related risks in good time and without delay, thus ensuring market transparency, customer confidence and market discipline at as high a level as possible;

3.4. promotion of public awareness of financial services and products. The Commission will continuously see to it that the information concerning the nature of financial services and products and related risks is available to the customers of the financial and capital market participants, especially to customers with a less than sufficient level of professional education in financial matters, so that customers can choose the relevant financial services or products on the basis of sound and reasoned decisions; and

3.5. protection of the interests of financial and capital market customers. The Commission will encourage the financial and capital market participants to ensure that the level of services provided to their customers is of the highest quality and in conformity with ethical norms.

4. Activities of the Commission Pertaining to the Implementation of Objectives:

4.1. to issue regulatory enactments and ordinances binding on market participants;
4.2. to license financial and capital market participants as well as individual financial products; to grant permits for the increase of capital, changes in the composition of shareholders, etc.;
4.3. to control the implementation of regulatory enactments and ordinances;
4.4. to compile, analyse and publish information concerning the financial and capital market (a quarterly report to the Bank of Latvia and the Ministry of Finance, an annual report to the *Saeima* [1], monthly statistics);
4.5. to prepare proposals regarding improvements to regulatory enactments and their harmonisation with EU regulations;
4.6. to carry out risk assessment at the level of an individual financial market participant and an individual financial market sector as well as at the level of the entire system;
4.7. to ensure the asset accumulation and management of the deposit guarantee fund and the fund for the protection of the insured, and the payment of compensations from such funds; and
4.8. to co-operate with foreign financial and capital market supervisory authorities, international financial organisations, the Bank of Latvia, the Ministry of Finance of the Republic of Latvia and to provide methodological assistance to the Office for the Prevention of Laundering of Proceeds Derived from Criminal Activity.

[1] Parliament of the Republic of Latvia.

REGULATORY REQUIREMENTS GOVERNING THE FINANCIAL AND CAPITAL MARKET

By the inception of the Commission on 1 July 2001, immense work had already been completed setting up a framework of regulatory requirements governing activities of the financial and capital market and its participants, which, according to an opinion delivered by the International Monetary Fund, in all its relevant aspects conforms to the requirements of EC directives and recommendations of international financial supervisory organisations.

In the second half of 2001 the Commission, as required by the Law on the Financial and Capital Market Commission, approved 82 regulatory documents (for the most part it involved re-approving the regulatory enactments issued by the Securities Market Commission, the Insurance Supervision Inspectorate, the Bank of Latvia, the Deposit Guarantee Fund, and the Cabinet) governing the activities of financial and capital market participants and the procedures for calculating the relevant indicators as well as those for preparation of annual accounts. Within the course of re-approval of these documents, amendments to the regulatory requirements were made and harmonisation of requirements regulating the operation of the various financial and capital market sectors was carried out.

In the second half of 2001, the Council of the Commission approved 82 regulatory documents governing the activities of financial and capital market participants.

Principal Regulatory Enactments Issued by the Commission

On 23 November 2001, the Council of the Commission approved the Guidelines for Developing Procedures for Identifying Clients and Unusual and Suspicious Financial Transactions that replaced the Guidelines for Developing Procedures for Identifying Suspicious Financial Transactions approved by the Board of Governors of the Bank of Latvia on 13 July 2000. The new Guidelines pertain not only to credit institutions but also to credit unions, brokerage firms, investment companies, insurers, depositories, stock exchanges and private pension funds.

The Regulation on the Annual Accounts of Banks approved by the Council of the Commission replaces the Guidelines for Annual Accounts of Credit Institutions approved by Resolution No. 36/5 of 14 November 1996 of the Board of Governors of the Bank of Latvia. Said regulation has been prepared taking into account amendments made to IAS since 1996 as well as amendments No. 2001/65/EEC to EC Directive No. 86/635/EEC on the Annual Accounts and Consolidated Accounts of Banks and Other Financial Institutions. This regulation provides for the procedures regarding classification of financial assets and financial liabilities according to their type and their initial recognition in the balance sheet, as well as for the procedures regarding subsequent valuation in accordance with the requirements of IAS 39. Moreover, the contents of notes to financial statements of a bank has been expanded by requiring the provision of qualitative and quantitative information concerning material risks in banking operations, including market risk.

The Regulation on the Annual Accounts of Credit Unions and the Regulation for the Calculation of Indicators Characterising the Operation of Credit Unions, which have been formulated in accordance with the requirements of the Law on Credit Unions, determine the requirements for drawing up annual accounts with regard to the volume and type of operations of credit unions and the procedures for assessing compliance with regulatory requirements and submitting the relevant accounts.

On the basis of an analysis of the progress of re-approving and harmonising the regulatory requirements, a detailed plan was worked out for the year 2002 in order to draft new regulatory requirements and improve some of the effective documents. Some minor nonconformities to EU requirements and recommendations of international financial and capital supervisory organisations will be eliminated and harmonisation of requirements regulating various financial and capital market sectors accomplished.

Formulation of Draft Laws

In 2001, the Commission participated in the formulation of several draft laws pertaining to the supervision of the financial and capital market and its participants. The formulation of the Law on the Protection of Investors, and amendments to the Law on Natural Person Deposit Guarantees, the Law on the Financial and Capital Market Commission, the Law on Credit Institutions and the Law on Securities, were some of the major projects. The Commission, in collaboration with the Bank of Latvia and the Association of the Latvian Commercial Banks, began the work on preparing draft laws on the out-of-court settlement of disputes and settlement finality.

The Law on the Protection of Investors ensures the implementation of the requirements of EC Directive 97/9/EC on Investor-Compensation Schemes, establishing a scheme for the protection of investors that, in cases where the providers of investment services are not able to meet their obligations, will entitle the investor to compensation. Its purpose is to compensate for any default on obligations in the amount of 90% of the value of irreversibly lost financial instruments, or losses caused by a non-executed investment service. Said law came into effect on 1 January 2002.

The amendments to the Law on Natural Person Deposit Guarantees, which will become effective on 1 January 2003, provide for the implementation of the requirements of EC Directive 94/19/EC on Deposit-Guarantee Schemes. The present applicable Law on Natural Person Deposit Guarantees sets forth only guarantees for deposits made by natural persons, whereas said directive determines the application of a deposit-guarantee scheme to both natural and legal persons.

Amendments to the Law on the Financial and Capital Market Commission harmonised the provisions of this law with those of the Law on Credit Unions adopted by the Saeima on 29 March 2001 and set forth the procedures for financing of the Financial and Capital Market Commission in the transitional period until full financing by the financial and capital market participants is provided. Amendments to this law came into effect on 1 January 2002.

Amendments to the Law on Securities implemented the requirements of EC Directive 93/22/EEC on Investment Services in the Securities Field. Said law stipulates that henceforth any company intending to perform intermediary activity in securities has to hold a licence, irrespective of whether the customer has instructed the intermediary to transact in Latvian or foreign securities. The amendments took effect on 1 January 2002.

Amendments to the Law on Credit Institutions have been formulated in order to implement the requirements of EC Directive 95/26/EC. The purpose of the amendments is to improve the overall supervision of credit institutions and grant the Commission relevant powers to prevent close links between a credit institution and third party in cases where such links might jeopardise the financial stability of the credit institution or restrict the supervisory body from performing functions prescribed by said law. The Commission also formulated amendments to the Law on Credit Institutions that will implement the "single license" principle with respect to setting up branches of banks registered in EU and European Economic Area countries and providing financial services in Latvia and vice versa. As a result of the introduction of the "single license" principle, a bank registered in a relevant country will not have to receive an operating licence in the country where it intends to open a branch or provide financial services. This provision is expected to take effect on 1 January 2003. The establishment of a new institution, creditors' meeting, is also under way to streamline banking insolvency procedures.

LICENSING

One of the most significant functions of the Commission is to issue or, in cases where the financial and capital market participants fail to comply with law or regulatory requirements, suspend or cancel special permits (licences) and certificates for operating in the financial and capital market.

At the end of 2001, there were 22 licensed banks and one branch of a foreign bank (the Latvian branch of *Nordea Bank Finland Plc*) and 22 credit unions in Latvia.

In 2001, credit institution licences were issued to two banks (the joint-stock company *Akciju komercbanka Baltikums* and the joint-stock company *Reģionālā investīciju banka*) and five credit unions (*Pūres Kooperatīvā krājaizdevu sabiedrība*, *Straupes Kooperatīvā krājaizdevu sabiedrība*, *Kandavas novada Kooperatīvā krājaizdevu sabiedrība*, *Kooperatīvā krājaizdevu sabiedrība Āgenskalns R*, *Salas Kooperatīvā krājaizdevu sabiedrība*). One banking licence was revoked as a result of a bank's reorganisation (the joint-stock company *Saules banka* was acquired by the joint-stock company *Rietumu Banka*).

Market concentration in the insurance sector continued. Licences of four insurance companies were cancelled. The licences of insurance companies *Alterna*, *Alterna Viva* and *Latgarants* were cancelled due to their reorganisation as they were acquired by other joint-stock insurance companies. Participants in the mutual insurance cooperative society *Solidaritāte* took a decision to wind up. As a result, the market comprised 21 insurance companies at the end of 2001. Insurance companies extended the range of services offered to customers and 126 new insurance products (policies) were registered as a result.

At the end of 2001, there were 28 insurance brokerage firms in Latvia. New licences were issued to seven companies, whereas licences of three insurance brokerage firms were cancelled. Interest in insurance brokerage activities was on the rise in the reporting year, resulting in 44 certificates issued for brokerage operations to natural persons. Seven certificates were cancelled, since their holders discontinued their brokerage activities. At the end of 2001, there were 139 registered insurance brokers in Latvia.

In the reporting year, eight insurance agencies were registered, whereas five insurance agencies were excluded from the register; the resulting total was 46 registered insurance agencies at the end of the year. At the end of 2001, the insurance market comprised 7 231 insurance agents. Within the year, the register of insurance agents included 1 136 agents, whereas 175 agents were struck from it.

As in 2001 no new private pension fund was set up, their number remained unchanged year-on-year, i.e., four funds. The number of investment companies likewise remained four. In the reporting year, an investment company operating licence was issued to the investment company *Optimus Fondi*, but the licence of one investment company, the joint-stock company *Vega Fondu Pārvalde*, was cancelled. In 2001, the number of registered investment funds likewise remained unchanged: five, as a result of registering one new investment fund, the open-end investment fund *Valsts Obligāciju fonds*, and cancelling the certificate of the open-end investment fund *Vega Baltijas Sabalansētais fonds*.

In the reporting year, the Commission issued a licence for intermediary activity in the securities market to five credit institutions (the joint-stock companies *Latvijas tirdzniecības banka*, *VEF banka*, *Ogres komercbanka*, *Akciju komerc-*

banka Baltikums and *Reģionālā investīciju banka*) and one brokerage firm (the joint-stock company *LHV Securities*). Due to reorganisation, a licence of one credit institution was cancelled. Consequently, by the end of the year, 27 intermediaries had obtained licences: 19 credit institutions and 8 brokerage firms.

In 2001, professional securities market specialist certificates were issued to 134 natural persons, for 558 specialists, the validity term of their certificates was extended, whereas two specialists had their certificates cancelled. 86 professional securities market specialists expressed no intention to extend the validity term of their certificates. As a result, the securities market comprised 687 certified professional securities market specialists at the end of 2001.

SUPERVISION

The purpose of the supervision of financial and capital market participants is to duly establish causes of possible problems that may arise in relation to their activities and, within the scope of competence of the Commission, to take preventive measures and decrease the possible effects of a participant's problems on the entire financial and capital market.

When supervising financial and capital market participants, particular attention was devoted to their compliance with special laws and regulations of the Commission. The supervision of participants is based on an off-site analysis of financial statements and prudential reports and on-site examinations.

When carrying out the supervision of market participants, the Commission staff had access to information regarding all market sectors and participants. This allows to conduct an examination of activities performed by an individual market participant in all sectors more effectively, to determine groups of connected persons in the financial market and to carry out an examination of the entire financial group.

In the reporting year, 108 exsaminations of activities of financial and capital market participants were conducted.

Banks

One of the tasks of the Commission is to ensure ongoing and all-embracing banking supervision by performing the following functions:
1. to analyse and assess indicators characterising banking activities and risk management policies. Within the period of operation of a bank, constant attention is paid to the qualitative and quantitative changes in its indicators as well as to its compliance with prudential requirements regulating banking activities on the basis of both individual and consolidated financial statements;
2. to analyse policies and procedures submitted by banks regarding risk management of new products and services;
3. to conduct examination of banking operations; and
4. where necessary, to carry out special purpose examinations of banks focusing on particular financial services provided by the bank (lending, management of trading book, performance of trust operations) and the compliance with particular regulatory requirements.

In 2001, 25 examinations of banking operations were conducted by the Commission staff. As in previous years, special attention was paid to the evaluation of asset quality and the analysis and evaluation of the internal control system.

In 2001, the amount of issued loans substantially increased, therefore, particular attention was paid to the evaluation of the credit risk management system (identification, measuring, monitoring and control) of banks during examinations in order to duly identify possible shortcomings and problems related to loan repayment. The strategy, policies and procedures regarding the granting of loans and their ongoing supervision were also assessed.

On 1 January 2001, the Regulation for Calculating Capital Adequacy determining the capital requirement for the market risk in the trading book of credit institutions came into force. The Commission staff evaluated the policies and procedures for the trading book management of banks and, when carrying out examinations, assessed their adequacy and observance in practice.

In 2001, six banks, which, in accordance with the requirements of the Law on Credit Institutions and the Regulation for Consolidated Supervision of Banks, form part of a banking group, were subject to supervision on the basis of consolidated financial statements. They must comply with regulatory enactments on the basis of consolidated financial statements. Examinations of such banks also include mandatory examinations of undertakings belonging to consolidation groups with the view of ascertaining whether they have established an efficient internal control system ensuring the preparation of adequate information for the needs of supervision as well as a risk management system enabling the bank to continuously control risk transactions within a group.

Insurance Companies

The Commission performed the monitoring of risks related to operations of insurance companies and the identification of problems as well as determined measures for their prevention. The supervision process of insurance companies consists of two parts – the Commission staff analyse monthly and quarterly financial statements and reports on insurance activities of insurers as well as conduct on-site examinations of activities of insurance companies.

In 2001, a total of 42 examinations (including 7 full-scope) were carried out in insurance companies. During examinations, compliance with the Law on Insurance Companies and their Supervision as well as with regulations issued by the Commission was checked. In 2001, particular attention was paid to investments made by insurers and their conformity to insurance obligations. The Commission staff, on a regular basis, monitored the performance indicators of insurers, tendencies towards changes in such indicators and, where necessary, specified measures to be taken to eliminate deficiencies.

Other Financial and Capital Market Participants

In 2001, 17 examinations were conducted in credit unions, 7 in pension funds, 4 in investment companies, and 13 in brokerage firms and banks performing intermediary activity.

When conducting examinations of the operation of pension funds and investment companies, the policies and procedures of pension plans and investment funds, the quality of assets and the compliance with restrictions specified by law, also, the conformity of functions of asset management and custody with the laws of the Republic of Latvia and regulations of the Commission, were assessed.

When supervising activities of Latvian issuers, attention was paid to their compliance with the Law on Securities and regulations of the Commission. The Commission staff saw to it that issuers duly disclosed any material information and published annual accounts with a view to protect the rights of minority shareholders and to provide timely information on recent developments in the activities of public companies.

When conducting examinations of intermediary activity and continually monitoring exchange and off-exchange transactions in securities, specific attention was focused on possible cases of misuse of insider information.

INTERNATIONAL CO-OPERATION

International Institutions

In 2001, the Commission actively co-operated with major international organisations in the field of the financial and capital market supervision: the Basel Committee on Banking Supervision, the International Association of Insurance Supervisors (IAIS), the International Organisation of Securities Commissions (IOSCO) and the International Commercial Crime Bureau (ICCB).

In 2001, the Commission promoted the co-operation with the International Monetary Fund, the Organisation for Economic Co-operation and Development and the International Network of Pension Regulators and Supervisors (INPRS).

Co-operation with the European Union

In 2001, the Commission actively participated in the processes related to the integration of Latvia into the EU by submitting proposals for the harmonisation of laws and regulations with EC directives and by formulating regulatory requirements that would enhance conformity of the requirements regulating financial market activities to EU norms. At the request of the EU, transposition tables were prepared, which will enable EU experts to assess the conformity of Latvian laws and regulations to the EU *acquis communautaire* in the field of finance.

In 2001, fruitful co-operation was developed with the Directorates-General for Internal Market and Economic and Financial Affairs of the European Commission, which assisted in efficient harmonisation of the Republic of Latvia regulatory enactments with the EU *acquis communautaire*.

Latvian Financial Sector Assessment Programme

Within the framework of the Financial Sector Assessment Programme, the World Bank and the International Monetary Fund gave an evaluation of the Latvian financial sector. A report prepared by experts of the Programme included a positive opinion on the regulatory environment of the banking, insurance and securities market as well as the course of pension system reforms. The report underscored the stability of the macroeconomic environment that ensured favourable preconditions for further development of the financial sector. It noted that the regulatory basis governing activities of financial market participants, which was formed by taking into account Latvia's aim to enter the EU, had improved considerably in recent years. The evaluation concluded that Latvia was largely compliant with the Basel Committee Core Principles for Effective Banking Supervision. The finding was similar for the insurance sector where supervision was adequate and Latvia was largely observant of the IAIS Core Principles. The Principles of Securities Regulation of IOSCO and the OECD Principles of Corporate Governance were also largely implemented. Latvia exhibited a high degree of transparency in virtually all of the areas in which it had been assessed (banking, insurance, and securities market supervision; and in the spheres of monetary policy and the payment system).

Also, preparatory work taken on to establish uniform financial market supervision has been highly evaluated. The positive evaluation of the Latvian financial sector confirmed the conformity of the requirements regulating activities of financial market participants and the supervision practice to international standards.

Co-operation with Foreign Financial Supervisory Authorities

12 information exchange agreements with financial supervisory authorities of various countries were concluded.

The Commission co-operated with several foreign financial supervisory authorities. In 2001, closer co-operation in the form of agreements on mutual exchange of information (Memoranda of Understanding) was started with the Bank of Belarus and the Swedish Financial Supervisory Authority in the field of credit institution supervision and the Luxembourg Financial Supervisory Authority (*Commission de Surveillance du Secteur Financier*), the Polish Securities and Exchange Commission and the Icelandic Financial Supervisory Authority in the field of the credit institution, insurance and securities market supervision. Preparation of an information exchange agreement with the Finnish Insurance Supervisory Authority was also commenced. In total, 12 information exchange agreements with financial supervisory authorities of various countries were signed. In the preceding years, agreements on the exchange of information in the field of credit institutions were entered into with the Bank of Lithuania, the Bank of Estonia, the Finnish Financial Supervisory Authority, and the German Supervisory Authority for Credit Institutions (*Bundesaufsichsamt für das Kreditwesen*), and agreements on the exchange of information in the field of securities market were signed with the Financial Supervisory Authorities of Denmark and Sweden, and the Securities Market Commissions of Lithuania and Estonia.

In 2001, an agreement on co-operation with the Swedish Financial Supervisory Authority was prepared, which provided for the sharing of experience in matters related to the supervision of financial and capital market participants.

OPERATION OF FINANCIAL AND CAPITAL MARKET PARTICIPANTS

Operation of Banks

At the end of 2001, the banking sector of Latvia comprised 22 banks and one branch of a foreign bank, the Latvian branch of *Nordea Bank Finland Plc*. In 2001, the aggregate paid-up share capital of banks increased by 17.6% and amounted to 236.9 million lats at the end of the year. The share of foreign capital in the paid-up share capital of banks accounted for 67.8%, a year-on-year decrease of 2.1 percentage points. Foreign shareholders owned more than 50% of the bank's share capital in 10 banks and the market share of these banks comprised 65.2% of the banking sector's total assets. Five banks were subsidiaries of foreign banks.

In 2001, the share of the Estonian and German capital in the share capital of Latvian banks continued to grow (by 1.0 and 5.0 percentage points, respectively). This was related to the consolidation of activities of the Estonian bank *Hansapank*, a subsidiary of the Scandinavian bank *ForeningsSparbanken AB* (*Swedbank*), and the German bank *Norddeutsche Landesbank Girozentrale*, in the banking sector of Latvia (see Chart 1).

The Latvian Government is still the only shareholder of the joint-stock company *Latvijas Hipotēku un zemes banka*; its share in total assets of the banking sector made up 3.2% as at 31 December 2001. The Government-owned share in the joint-stock company *Latvijas Krājbanka* decreased to 32.0% (its share in total assets of the banking sector – 4.1%).

In the reporting period, the assets of banks grew by 760 million lats, or 28.2% reaching 3,458.5 million lats by the end of the period. As a result of the development of the banking sector, the structure of banks' assets changed. As loans increased by 50.5%, their share in the banks' assets rose from 40.3% to 47.3% (see Chart 2). The share of five major banks increased and amounted to 66.2% of assets, 73.0% of loans, and 69.0% of deposits (see Chart 3). The ratio of loans issued (to residents) to gross domestic product had grown from 21.7% in 2000 to 30.1% by the end of 2001*.

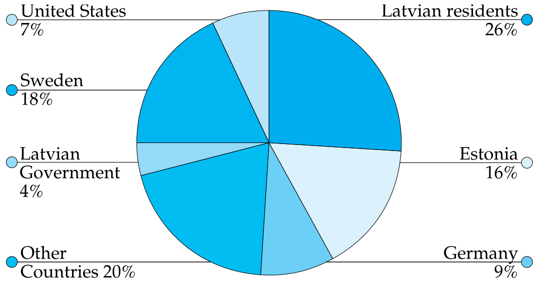
The national economy was actively engaged in borrowing. At the end of 2001, 85.9% of total loans were granted to domestic borrowers. The rapid growth of the national economy determined the increase in loans in all the major national economy sectors: 17.7% in manufacturing, 31.4% in trade and 22.0% in transport, storage and communications, whereas the amount of loans issued to construction increased as much as 2.3 times. Mortgage lending developed rapidly. Its growth rate in the reporting period amounted to 112.1%, consequently, the share of mortgage loans in the loan portfolio of banks increased from 10.9% at the beginning of 2001 to 15.2% at the end of 2001.

In 2001, the amount of lending substantially increased and the stable tendency of the loan quality to improve continued. By the end of the year, banks had assessed 95.8% of the loan portfolio as standard and only 1.4% - as close-watch. The share of non-performing loans (substandard, doubtful, lost) in the total of loans granted to non-banks dropped from 4.5% to 2.8% (see Chart 4), and their volume decreased as a result. In the reporting year, the ratio of specific provisions for non-banks to the total of loans granted to non-banks decreased by 1.2 percentage points and amounted to 1.7% at the end of 2001,

Chart 1

GEOGRAPHICAL BREAKDOWN OF SHARE CAPITAL OF BANKS

(at end of 2000; %)



(at end of 2001; %)

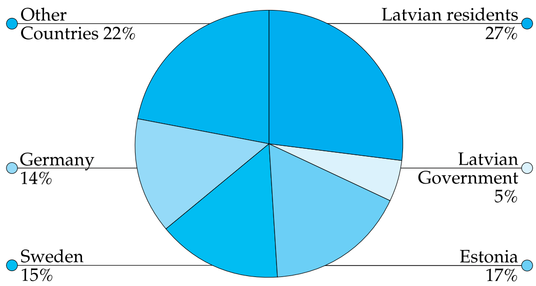
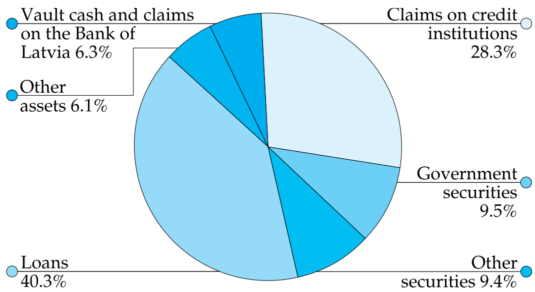


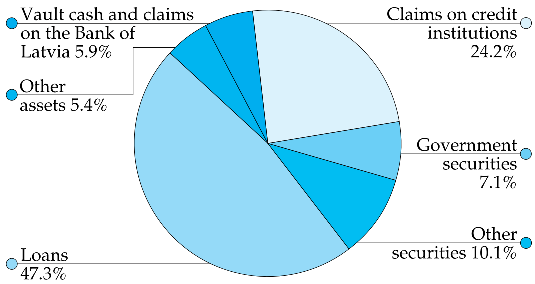
Chart 2

STRUCTURE OF ASSETS OF BANKS

(at end of 2000; %)



(at end of 2001; %)



* Gross domestic product, as estimated by the Republic of Latvia Ministry of Economy in 2001, was 4,666.1 million lats // Report on the Latvian National Economy Development. – Riga, December 2001.

Chart 3

MARKET SHARE OF 5 MAJOR LATVIAN BANKS

1998 to 2001 (at end of period; %)

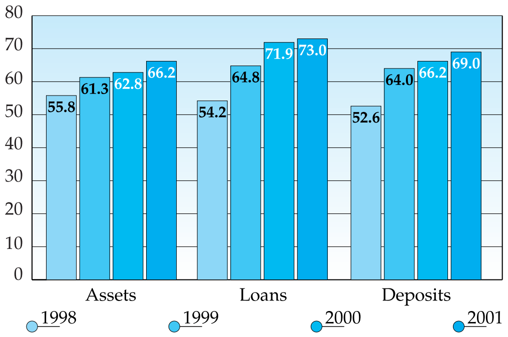


Chart 4

NON-PERFORMING LOANS OF BANKS

(as a percentage of total loans; %)

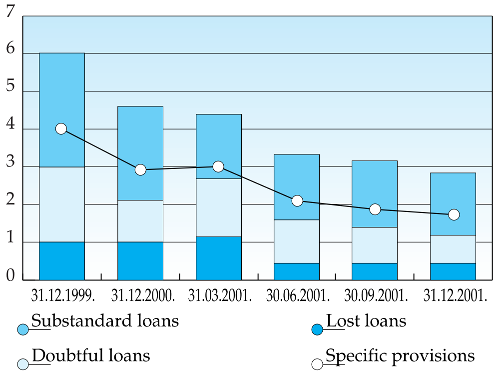
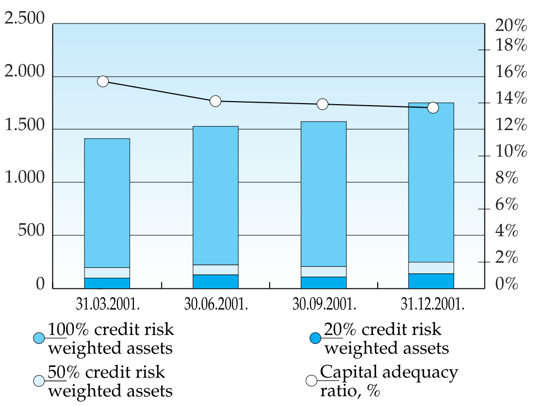


Chart 5

RISK-WEIGHTED ASSETS OF BANKS AND CAPITAL ADEQUACY RATIO

(in millions of lats, %)



attesting to the overall improvement of quality of the banking sector's loan portfolio. The changes in the term structure of loans in 2001 were caused by more extensive use of borrowing for the financing of working capital (commercial loans increased by 66.6%, reaching 42.4% of the loan portfolio) as well as by more extensive use of credit cards (credit card loans increased by 3.8 million lats, or 32.6%), thus the volume of short-term loans increased by 49.7%. The volume of long-term loans (more than 5 years) increased almost twofold, reaching 469.8 million lats, or 29% of the aggregate loan portfolio at the end of the reporting year.

In 2001, the amount of deposits grew by 24.9%, totalling 2,329.7 million lats. The deposits of residents grew by 25.1% and amounted to 1,121.7 million lats, including deposits of private persons, which grew by 40.8%, amounting to 557.4 million lats.

The Commission had determined that banks should maintain liquid assets (vault cash, claims on the Bank of Latvia, claims on credit institutions and liquid securities) in amounts sufficient to meet their obligations but not less than 30% of their total current liabilities. In the reporting year, the liquidity ratio of the banking sector ranged from 65% to 69% and accounted for 65% at 31 December 2001.

In 2001, the profit of the banking sector* reached 49.6 million lats, compared to 38.3 million in 2000. The main sources were income from the interest on loans issued to non-banks and fee and commission income: respectively 38.3% and 23.1% of total income. The efficiency of banks improved. In the reporting year, their efficiency coefficient of financial activity, i.e., the ratio of administrative expenses to net financial activity income, was 57.4, a 3.2 percentage point drop year-on-year. The return on equity (ROE) increased by 0.4 percentage points, reaching 19.0%, whereas the return on assets (ROA) slightly declined – from 1.6% in 2000 to 1.5% in 2001.

Ensuring maximum compliance with EC directives, capital adequacy calculations made by banks as of 1 January 2001 included not only the credit risk and currency risk capital requirement but also capital requirement for the position, commodities, settlement and counterparty risk inherent in the trading book. At 31 December 2000 the capital adequacy ratio of the banking sector was 14.3% (at 31 December 2001 – 14.2%) (regulatory requirement – 10%), but if capital adequacy calculations had been made according to the requirements for the year 2000, this ratio would have been 14.7%. Thus, in the reporting year, when including the risk capital requirement inherent in the trading book in capital adequacy calculations, the capital adequacy ratio of the banking sector decreased by 0.5% percentage points. In the reporting year, the share of a total of market risk capital requirements in the total of all capital requirements was comparatively small and varied from 3% to 5%. The main risk for banks was constituted by the credit risk of the banking book. At the end of 2001, the ratio of capital to total assets remained unchanged year-on-year – 10.6%; however, the rapid increase in the amount of the loan portfolio of banks brought about an increase in the total amount of the banking sector assets having a 100% risk weighting (see Chart 5).

Operation of Credit Unions

In the reporting period, there were 22 credit unions in Latvia. Their assets rose by 61%, reaching 1.65 million lats by 31 December 2001 (0.05% of the banking sector assets) (see Chart 6). This increase resulted largely from an influx of credit union member deposits, which by the end of 2001 had grown by 81.7% (in 2000 – 47.5%), amounting to 1.0 million lats, or 61.1%, of total liabilities of credit unions.

The main type of credit union activity was lending to their members. At the end of 2001, the aggregate loan portfolio of credit unions comprised 74.3% of their assets.

* non-audited profit

In the reporting period, the volume of loans increased by 47.4% and totalled 1.2 million lats on 31 December 2001. Credit unions issued short-term (up to one year) and medium-term (from 1 to 5 years) loans, mainly for the purchase of consumer goods. In 2001, the amount of medium-term loans increased more than threefold, reaching 21.9% of total loans (at the end of 2000 – 10.5%).

In 2001, the quality of the loans issued improved. At the end of the reporting year, the share of non-performing loans in the loan portfolio was 2.9% and the amount of specific provisions 7.7% of total loans (see Chart 7). Such loan quality improvements were promoted by the precautionary loan policy implemented by credit unions.

In 2001, credit unions showed a profit in the amount of 20.3 thousand lats, 2.9 times more than in 2000 (6.9 thousand lats). The main source of income was income from the interest on loans issued to members of credit unions (53.9% of total income). As a result of loan quality improvements, income was also derived from the increase arising from a decrease in provisions (26.0% of total income).

In the reporting period, the capital adequacy ratio of the credit union sector was much higher than the specified minimum capital adequacy requirement (10%) and ranged from 36% to 43%; also, liquid assets were maintained in sufficient amounts to meet obligations (liquidity ratio ranged from 61.0% to 116.0%; regulatory requirement – 30%).

Operation of Insurers

At the end of 2001, there were 21 insurance companies in Latvia, whereof 6 were involved in life insurance and 15 in non-life insurance operations. Five (two life insurance and three non-life) insurance companies were operating as subsidiaries of foreign insurers; the share capital of three insurance companies was wholly made up of investments of various foreign insurance companies, moreover, the share capital of three non-life insurance companies comprised a substantial foreign participating interest (more than 10%). At the end of 2001, the total amount of direct investments of foreign legal and natural persons in the share capital of insurance companies amounted to 20 million lats, or 52% of the paid-up share capital of insurance companies.

In the reporting year, the increase in the amount of gross claims paid was larger than the increase in the amount of gross premiums written. In 2001, the gross premiums written by insurance companies accounted for 96.9 million lats, 1.3 million lats more than in the year 2000, while gross claims paid accounted for 37.6 million lats, 3.4 million lats more than in the previous year (see Chart 8).

The development of insurance brokerage services affected the prices of products of insurance companies and resulted in tighter competition among insurance companies. At the end of 2001, there were 28 insurance brokerage companies in the market. As a result, 12.6 million lats worth of premiums were written by intermediation of insurance brokerage companies. The share of gross premiums written through brokerage firms constituted 13% of total gross premiums written, whereas the share of gross premiums written through brokerage firms in 2000 constituted 11% of total gross premiums written.

The insurance penetration gradually decreased, thus at the end of 2001 it was the same as in 1997 – 2.1%* .

Chart 6

ASSETS AND DEPOSITS OF CREDIT UNIONS

(at end of period; in thousands of lats)

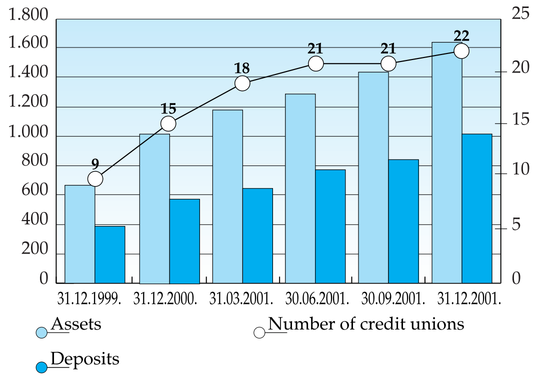


Chart 7

LOAN PORTFOLIO OF CREDIT UNIONS

(%)

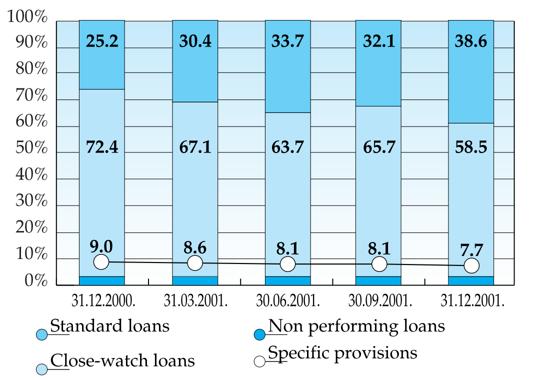
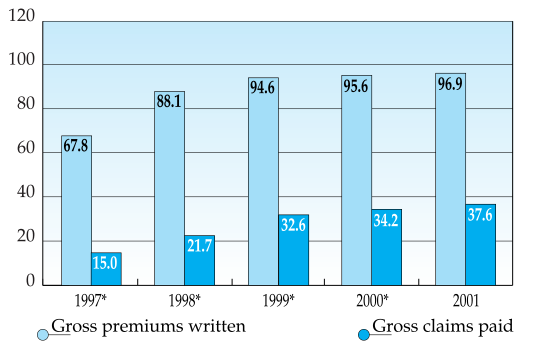


Chart 8

GROSS PREMIUMS WRITTEN AND GROSS CLAIMS PAID

(at end of period; in millions of lats)



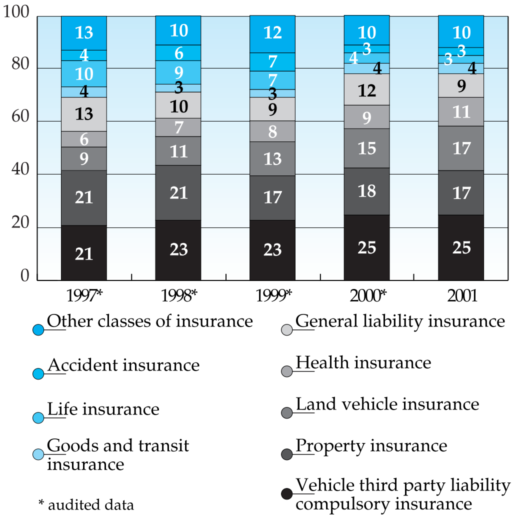
* audited data

* Gross domestic product for 2001, as estimated by the Republic of Latvia Ministry of Economy, was 4,666.1 million lats.

Chart 9

GROSS INSURANCE PREMIUMS WRITTEN BY CLASSES

(at end of period; %)

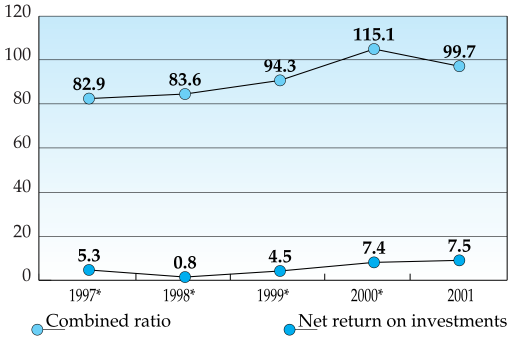


* audited data

Chart 10

NET RETURN ON INVESTMENTS AND COMBINED RATIO OF EXPENSES

(%)

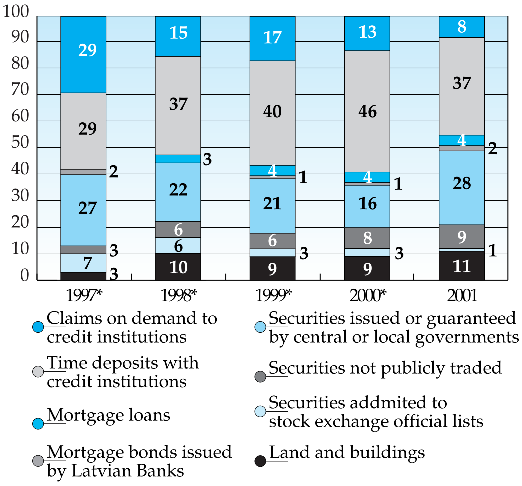


* audited data

Chart 11

STRUCTURE OF INVESTMENTS COVERING NET TECHNICAL RESERVES

(%)



* audited data

Simultaneously, the second indicator characterising the importance of the industry for the national economy – the insurance density – rose by 0.8 lats, reaching 41.2 lats in 2001. The increase in this indicator can largely be attributed to the decrease in the number of residents within the last years.

In 2001, there were no significant changes in the portfolio of gross premiums written by insurance companies. Non-life insurance still prevailed and the share of gross premiums written for life insurance dropped from 4% in 2000 to 3% in 2001 (see Chart 9).

The combined ratio dropped from 115.1% in 2000 to 99.7% in 2001 (see Chart 10). Taking into account the fact that the net return on investments in 2001 was 7.5%, the actual ratio characterising the result of operations of insurers was 92.2% (in 2000, this ratio was 107.7%).

As at 31 December 2001, the net technical reserves of insurance companies were 44.9 million lats. The technical reserves were fully covered by investments provided for by the Law on Insurance Companies and their Supervision, and 97% of a total of these investments were made in Latvia. The investment portfolio structure covering technical reserves was aimed at maximum risk reductions. The bulk of investments were made up of time deposits with credit institutions (37%) and securities issued and guaranteed by governments or local governments (28%) (see Chart 11).

Operation of Pension Funds

In 2001, there were four pension funds in Latvia. Three open funds and one closed pension fund offered a total of 14 pension plans. In Latvia, the first licence for the operation of a private pension fund was issued on 23 October 1998. A pay-as-you-go system, a second-tier pension scheme and private pension funds make up a three-pillar pension system in Latvia.

The year 2001 was successful for the development of private pension funds and it was characterised by the following indicators: the number of participants in the third tier increased 2.5 times and amounted to 17.4 thousand, or 1.7% of the average number of employed persons in Latvia, at the end of the year;
- the amount of pension plan assets increased twofold and comprised 9.5 million lats at the end of 2001;
- the investment policy of pension plan assets continued to be rather conservative, retaining maximum restrictions on risks. Of pension plan assets, 93% were invested in Latvia and the remaining 7% in the Baltic and OECD countries. The additional accrued capital was mainly invested in fixed-income debt securities (see Chart 12), thus the share of these investments rose to 61% of pension plan assets. The amount of investments in time deposits with credit institutions remained unchanged – 3 million lats; the share of these investments amounted to 31% of the total of pension plan assets at the end of 2001.

The state-funded pension scheme (the second-tier pension system) was launched on 1 July 2001. The participation in the second-tier pension system was mandatory for those persons who had not reached the age of 30 before 1 July 2001, whereas persons at the age from 30 to 49 years joined voluntarily. At the end of the reporting year, 280 thousand participants took part in the second-tier, or state-funded pension scheme, of these, 26.7 thousand participants had joined voluntarily*. Until 1 January 2003, assets of the second-tier pension system will be managed by the State Treasury but, as of 2003, the management will also be entrusted to private asset managers licensed by the Commission.

* Provisional data of the State Social Insurance Agency.

Operation of Securities Market Participants

At the end of 2001, the Latvian securities market comprised the Riga Stock Exchange, the Latvian Central Depository, 8 brokerage firms and 19 banks (intermediary companies) providing brokerage services as well as four registered investment companies managing four investment funds (three open-end funds and one closed-end fund).

In the reporting year, the total turnover of the Riga Stock Exchange amounted to 531.4 million lats, or 4.5% less than in 2000, which was related to a decrease in the share turnover. In 2001, the capitalisation of the stock market increased by 21.8%, amounting to 438.6 million lats; the stock market liquidity (the ratio of turnover to capitalisation), however, dropped from 46.8% to 23.5%.

The Dow Jones Riga Stock Exchange index (in US dollars) rose by 38.38% and amounted to 172.46 points at the end of 2001. The depth of the stock market (the ratio of turnover to gross domestic product) increased from 8.3% in 2000 to 9.4%* in 2001.

At the end of 2001, the amount of securities registered with the Latvian Central Depository (in their face value) made up 652.0 million lats, including shares – 52.0%, government debt securities – 39.5%, corporate debt securities 7.4% and investment fund certificates – 1.1%. The term structure of government debt securities – in the amount of 257.5 million lats included: 3-, 6- and 12-month debentures – 11.7%, 2-year bonds – 5.8%, 3-year bonds – 27.5% and 5-year bonds – 55.0%. In the reporting year, government debt securities were issued in the amount of 31.9 million lats. At the end of 2001, the aggregated value of Latvian securities was 664.9 million lats, of which 56% were owned by Latvian investors and 44% by foreign investors. It should be noted that the Latvian Central Depository maintains the Initial Register for securities accounts created as a result of privatisation, which at the end of the reporting year included 68.0 thousand securities accounts that were not yet transferred to custodians.

At the end of 2001, there were 100 issuers of public securities in the Latvian securities market. Of the aggregate value of outstanding public equities, 19.8% were issued by *Ventspils nafta*, 12.2% by *Latvijas Unibanka*, 8.3% by *Latvijas Gāze* and 5.6% by *Rīgas transporta flote*.

In 2001, the Commission registered five issues of public securities in the amount of 10.4 million lats, including share issues of three privatised companies in the amount of 2.4 million lats and two mortgage bond issues in the amount of 8.0 million lats. One open-end investment fund issued investment fund certificates.

In the reporting year, the number of securities accounts held by intermediary companies, as well as the ratio of residents to non-residents in comparison with 2000 practically remained unchanged. At the end of 2001, there were 46 362 residents' accounts and 727 non-residents' accounts. The volume of the securities portfolio held by holders of securities accounts grew by 28.7% and amounted to 1,002.7 million lats at the end of the year, including equity securities at 36.3%, debt securities issued by public institutions at 36.5% and corporate debt securities at 27.2% (see Chart 13). Though in the reporting year the share of the securities portfolio held by Latvian residents diminished by 5.0 percentage points and at the end of 2001 accounted for 68.6% of the aggregate securities portfolio, the gross turnover of securities of residents increased quarterly, thus the 4th quarter turnover in comparison with 1st quarter turnover increased 2.7 times, reaching 2,220.4 million lats (see chart 14).

Chart 12

STRUCTURE OF PENSION PLAN ASSETS

(in millions of lats)

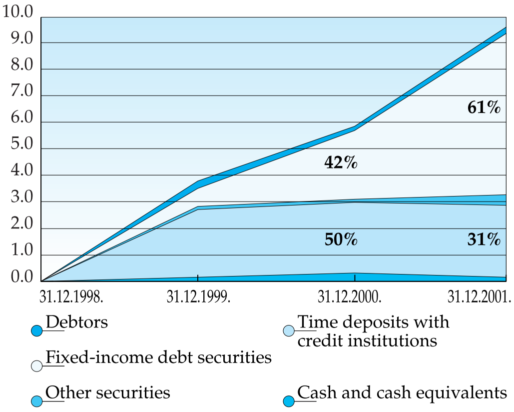


Chart 13

SECURITIES PORTFOLIO HELD BY LATVIAN INTERMEDIARY COMPANIES IN BREAKDOWN BY TYPE OF SECURITY

(in 2001; in millions of lats)

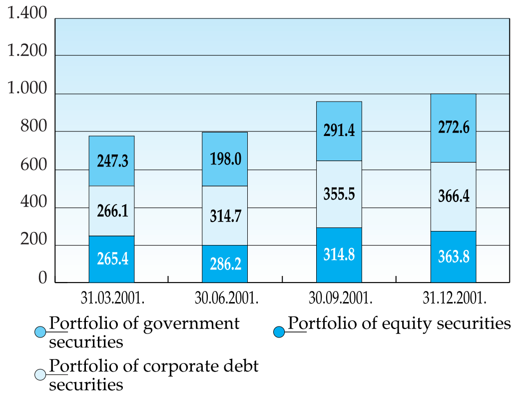
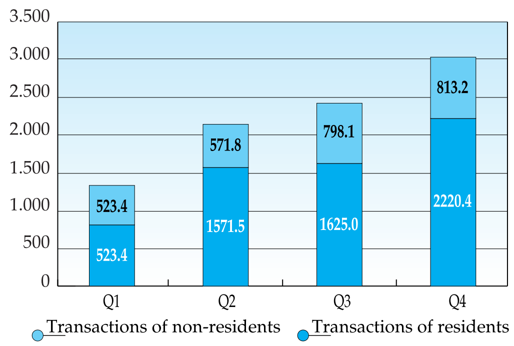


Chart 14

TRANSACTIONS OF RESIDENTS AND NON-RESIDENTS IN SECURITIES MARKET

(in 2001; in millions of lats)

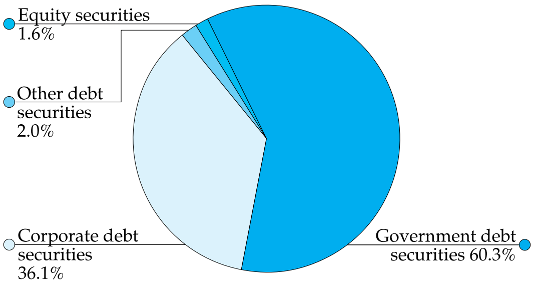


* The gross domestic product estimated by the Republic of Latvia Ministry of Economy in 2001– 4,666.1 million lats // Report on the Latvian National Economy Development. – Riga, December 2001.

Chart 15

SECURITIES PORTFOLIO OF INVESTMENT FUNDS IN BREAKDOWN BY TYPE OF SECURITY

(at end of 2000; %)



(at end of 2001; %)

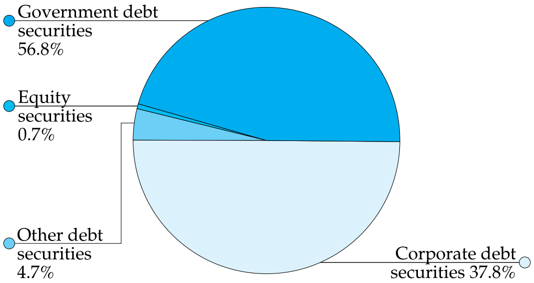
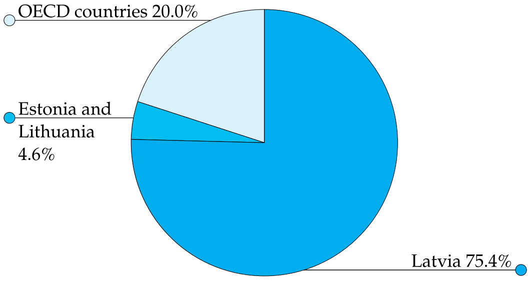


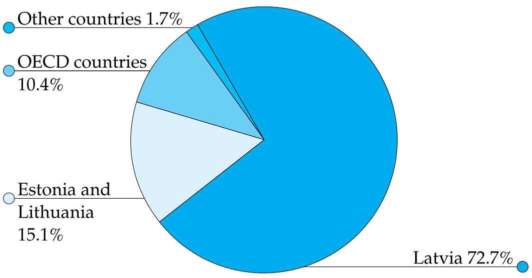
Chart 16

SECURITIES PORTFOLIO OF INVESTMENT FUNDS IN BREAKDOWN BY COUNTRY

(at end of 2000; %)



(at end of 2001; %)



In 2001, the most significant contributor to the turnover of public securities was the government debt securities, which contributed 78.6% to the total turnover of public securities.

From the beginning of 2001, assets of investment funds grew by 50.4%, or from 5,028.1 thousand lats to 7,561.4 thousand lats at the end of the period.

At the end of 2001, the securities portfolio of investment funds comprised 5,400.1 million lats. In the reporting year, the structure of the securities portfolio of investment funds changed. Investments in corporate debt securities increased 1.5 times, reaching 2,040.3 thousand lats at the end of the reporting period, thus comprising 37.8% of the securities portfolio (see Chart 15). In 2001, investments in government debt securities grew by 34.2% and comprised 3,063.0 thousand lats, or 56.8% of total securities, as at 31 December 2001.

In the reporting year, investment funds increased the amount of investments made in Estonia and Lithuania by 4.7 times, thus their share amounted to 15.1% of the aggregate securities portfolio at the end of 2001 (see Chart 16). Simultaneously, investments in Latvia decreased by 2.7 percentage points while investments in the OECD countries, by 9.6 percentage points, which on 31 December 2001 accounted for 3.9 million lats and 0.6 million lats, respectively.

In 2001, the increase in net assets as a result of investments constituted 395.3 thousand lats (in 2000 – 159.3 thousand lats).

REPORT OF THE COUNCIL OF THE FINANCIAL AND CAPITAL MARKET COMMISSION

The Commission commenced its activities on 1 July 2001. These activities are based on the strategy for the regulation and supervision of the Latvian financial and capital market approved by the Council of the Commission on 31 August 2001.

Pursuant to the Law on the Financial and Capital Market Commission, the Commission is administered by the Council whose composition in the year 2001 was as follows:

– Chairman	**Uldis Cērps**
– Deputy Chairman	**Jānis Brazovskis**
– members of the Council	**Jānis Placis**
	Gvido Romeiko
	Ludmila Vojevoda.

The chairperson and deputy chairperson of the Council are appointed by the *Saeima*, whereas the other three members of the Council are, in turn, appointed by the chairperson upon prior agreement of candidates with the Minister of Finance and the Governor of the Bank of Latvia. The Commission includes the following three departments:

– the Supervision Department;
– the Legal and Licensing Department;
– the Regulations and Statistics Department.

Members of the Council are simultaneously directors of departments of the Commission. In the reporting year, activities of the Commission were financed from payments of financial and capital market participants, the State budget and the Bank of Latvia in the amounts specified by the Law on the Financial and Capital Market Commission. The amount of payments of the State budget and the Bank of Latvia will gradually decrease in the next few years, and, eventually, activities of the Commission will be financed exclusively from the payments of financial and capital market participants. In the reporting year, the Commission did not provide any services for pay to the general public.

In 2001, the organisational and management structure of the Commission was fully set up in compliance with the functional division in order to ensure mutual co-operation and equal supervision quality in all financial and capital market sectors. At the end of 2001, the Commission had 95 employees.

In 2001, the Commission staff participated in workshops on financial and capital market supervision organised by the Joint Vienna Institute, the International Monetary Fund, the Bank of Austria, the Organisation for Economic Cooperation and Development (OECD), the International Network of Pension Regulators and Supervisors (INPRS) and the Financial Stability Institute. The Commission also participated in the Central European Mortgage Bonds Conference and the Danish-Latvian Mortgage Project and got acquainted with the work of the Danish Financial Supervisory Authority. The Commission staff improved their knowledge also in seminars organised by the Latvian, Lithuanian and Estonian Actuary Associations. In order to inform financial and capital market participants and the public of market developments and activities of the Commission, a web page of the Commission was set up on the Internet (www.fktk.lv).

In 2001, 25 meetings of the Council of the Financial and Capital Market Commission took place taking 82 decisions pertaining to the financial and capital market overall, 118 decisions pertaining to specific participants in the financial and capital market and 53 decisions approving internal enactments governing the internal procedures of the Commission. In 2001, an efficient internal control system was set up at the Commission. Major control procedures were approved and the documenting of all processes was carried out. In 2002, in order to increase the efficiency of the internal control system, the Commission will introduce a quality management system in conformity with international quality standard ISO 9001:2000.

The functions of the Commission include the regulation of the financial and capital market and its participants by controlling the implementation of laws and regulations of the Republic of Latvia and regulations of the Commission. In 2001, when supervising financial and capital market participants, particular attention was focused on compliance with special laws and other regulatory requirements. In the reporting year, 25 examinations were conducted at banks, 17 in credit unions, 42 in insurance companies, 7 in pension funds, 4 in investment companies and 13 in brokerage firms and at banks performing securities intermediary activity.

In order to foster the efficiency of the financial and capital market and to promote its stability, the Consultative Council of the Financial and Capital Market Commission (hereinafter – the Consultative Council) performed its activities pursuant to the Law on the Financial and Capital Market Commission. The Consultative Council is formed of representatives of the Commission and heads of public organisations (professional associations) of financial and capital market participants on the basis of the principle of parity. The Consultative Council has the right specified by said law to give its evaluation of the annual draft budget of the Commission, examine draft regulations and submit proposals to the Chairman of the Commission regarding improvement of the work of the Commission.

In the reporting year, the Consultative Council gave the Commission's work a positive evaluation. The Commission, complying with the requirements of law, has successfully implemented functions assigned to it in order to promote the stability and development of the financial and capital market.

In 2001, the Commission approved the budget and the work schedule for the year 2002, including the harmonisation of the Republic of Latvia laws and regulations with EC directives, the setting up of a single database of statistical, licensing and supervision information pertinent to market participants, the exchange of information with market participants in electronic form, and the introduction of an electronic record-keeping system as the main priorities.

MAJOR TASKS OF THE FINANCIAL AND CAPITAL MARKET COMMISSION FOR THE YEAR 2002

1. Supervision of the financial and capital market participants by making an analysis of financial statements and stock exchange information as well as by carrying out regular on-site examinations of activities of the market participants;

2. The "Peer Review" project, i.e., assessment of conformity of the Republic of Latvia laws and regulations to EU requirements that will enable EU experts to obtain a clear view of the transposition of EU directives into the laws and regulations of the Republic of Latvia, determining any possible non-conformities and formulating proposals regarding timely prevention of such non-conformities.

3. Assessment of the conformity of applicable laws and regulations to EU requirements, recommendations of international financial supervisory authorities and the best international practices, formulating, where necessary, proposals regarding improvements to regulatory requirements in order to prevent possible contradictions and discrepancies.

4. Building a combined database of statistical, licensing and supervision information pertinent to market participants as well as conducting an exchange of information with the market participants in electronic form.

5. Introduction of an electronic record-keeping system in order to improve the document formulation, circulation and storage at the Commission.

6. Introduction of a quality management system and certification in conformity with the international quality standard ISO 9001:2000.

7. Regular exchange of information between the Bank of Latvia and the Ministry of Finance regarding the financial and capital market.

FINANSU UN KAPITĀLA TIRGUS KOMISIJA

FINANCIAL AND CAPITAL MARKET COMMISSION FINANCIAL STATEMENTS FOR 2001

MANAGEMENT REPORT ON THE FINANCIAL STATEMENTS

In accordance with Article 3 of the Transitional Provisions of the Law on the Financial and Capital Market Commission, the Commission acquired assets and liabilities of the Insurance Supervision Inspectorate, the Securities Market Commission and the Deposits Guarantee Fund, as well as fixed assets granted by the Bank of Latvia.

In accordance with the Law on State Budget for 2001 and Decision No. 80/8 on Expenses of the Bank of Latvia for Establishment of the Financial and Capital Market Commission and Commencement of Its Activities issued by the Board of Governors of the Bank of Latvia on 16 November 2000, the Commission was granted funds for establishment and commencement of activities.

In compliance with Article 7 of the Law on the Financial and Capital Market Commission, financing for the Commission's activities and use of these funds was set in the Budget of the Financial and Capital Market Commission for the 6 months of 2001 approved by Decision No. 1/12 of the Council of the Commission on 6 July 2001.

As an autonomous public institution possessing State property, the Commission carried out accounting in accordance with the Law on Accounting and principles set by instructions issued by the State Treasury.

Financial statements of the Commission were prepared based on the principles set in Instruction No. 1 of the State Treasury for the Preparation of Financial Statements.

The Commission disclosed all assets and liabilities in a common balance sheet and revenues and expenses of the Commission's financing as well as revenues and expenses of the Deposits Guarantee Fund and the Fund for Protection of the Insured in a common statement of income and expenses.

In accordance with Article 6 of the Law on the Financial and Capital Market Commission, during the reporting period the Commission managed assets of the Deposits Guarantee Fund and the Fund for Protection of the Insured. Assets of the funds managed by the Commission, for the purposes of clearer perception, are disclosed separately in the balance sheet. A separate cash flow statement and a statement of income and expenses were prepared for the Deposits Guarantee Fund and the Fund for Protection of the Insured as separate notes to these financial statements.

As the Commission was granted funds for establishment and commencement of activities, funds used for these purposes were accounted separately. A separate cash flow statement and a statement of income and expenses were prepared for these funds and disclosed in the notes to the financial statements. The acquired assets will be used in further Commission's activities therefore these assets were disclosed in the total balance sheet.

The Commission has separately accounted for funds constituting financing of the Commission in accordance with Article 5 of the Transitional Provisions of the Law on the Financial and Capital Market Commission. A separate cash flow statement and a statement of income and expenses were prepared for these funds. The Commission's balance sheet discloses Commission's assets and liabilities, as well as assets and liabilities of the acquired institutions and liabilities and assets purchased for the funds intended for financing and commencement of the Commission's activities.

In accordance with Article 13 of the Law on the Guarantees of Deposits of Natural Persons and Article 97 of the Law on Insurance Companies and their Supervision, assets of the Deposits Guarantee Fund and the Fund for Protection of the Insured may be invested only in government securities of Latvia. In compliance with requirements of the Regulations on the Issuance of Treasury Bills approved by Order No. 285 of the Ministry of Finance issued on 11 April 1997 and terms of the agreement concluded between the Commission and the State Treasury on investment of funds of the Deposits Guarantee Fund and the Fund for Protection of the Insured in the Latvian Government securities at initial placement, during 2001, funds in the possession of the Commission were invested in the treasury bills of Latvia.

As the Commission's assets are State property in accordance with the Law on State and Municipality Procurement, tenders were organised for transactions performed by the Commission.
During 2001, the State Audit Office did not perform an audit of the Commission's activities.

On 21 November 2001, as a result of a price poll, SIA "KPMG Latvia", represented by Sworn Auditor Valda Užāne, was appointed the auditor of the Commission's financial statements for 2001.

Total Budget of the Commission

The assets of the Commission, including managed trust assets – the funds of the Deposits Guarantee Fund and the Fund for the Protection of the Insured – at the end of 2001 were 7,160,883 lats. Total revenues in the 6 months of 2001, which consisted of the funds for the establishment of the Commission and the Commission's regular financing revenues were 1,656,877 lats. Total expenses consisting of the establishment costs of the Commission and the operating expenses were 1,011,842 lats. Thereby, the excess of the total budget revenues of the Commission over the expenses in the reporting period was 645,035 lats. It consisted of the excess of revenues over expenses for ensuring Commission's activities of 105,964 lats and the excess of revenues over expenses for the establishment of the Commission and the financing for the commencement of its activities of 539,071 lats, which was explained by the large share of prepaid expenses and capital investments associated with the establishment of the Commission and commencement of its activities, which are depreciated and amortised over a longer period of time.

Financing for Establishment of the Commission and Commencement of Its Activities

In accordance with the cost estimate for the establishment of the Commission and commencement of its activities agreed between the Bank of Latvia, the Insurance Supervision Inspection and the Securities Market Commission on 14 November 2000, as well as the amendments to the above estimate on 26 June 2001, the Commission received financing of 884,200 lats for establishment of the Commission and commencement of its activities. Based on the Decision of the Board of Governors of the Bank of Latvia of 16 November 2000 No. 80/8, On Expenses of the Bank of Latvia for Establishment of the Financial and Capital Market Commission and Commencement of its Activities, additional financing of 12,000 lats was granted for a reserve, which was used in the amount of 6,299 lats. Overall financing for the establishment of the Commission and commencement of its activities was 888,299 lats – the Bank of Latvia granted funds of 688,299 lats and the State budget allocated 200,000 lats. The payments of the Bank of Latvia were reflected in the cash flow statement and the statement of income and expenses on the establishment of the Commission and commencement of its activities, but the payments from the State budget were included in the budget result of the establishment of the Commission and commencement of its activities (the payments were made until 30 June 2001), which was recognised in the balance sheet as at 1 July 2001. The excess of income over expenses stated in the statement of income and expenses on the establishment of the Commission and commencement of its activities was 539,071 lats, but excess of revenues over expenses in the cash flow statement was 61,885 lats. The money spent for commencing the operations of the Commission was 821,950 lats. Totally, 94% of the allocated financing was used for the Commission's establishment and commencement of its activities. The financing for commencement of the Commission's activities was utilised in accordance with the cost estimate.

Operations of the Commission in the 6 Months of 2001

In the 6 months of 2001, the revenues of the Commission were 968,578 lats and by 2% exceeded the forecasted revenues laid down in the budget approved by the Board of the Commission on 6 July 2001 (947,556 lats). Expenses of the Commission were 862,614 lats or 91% of the forecasted expenses (947,178 lats), from which 85% has been used for the staff remuneration and State compulsory social insurance contributions. In total, the revenues of the 6 months exceeded expenses by 105,964 lats.

Management of the Deposits Guarantee Fund and the Fund for the Protection of the Insured

In the reporting period, income of the Deposits Guarantee Fund amounted to 934,577 lats and income of the Fund for Protection of the Insured amounted to 77,000 lats. Income from investments of the Deposits Guarantee Fund was 132,248 lats, but income of the Fund for Protection of the Insured was 20,478 lats. Total assets of these funds increased by 1,164,303 lats or 25%: assets of the Deposits Guarantee Fund increased by 1,066,826 lats or 26%, but assets of the Fund for Protection of the Insured increased by 97,477 lats or 17%. At the end of 2001, net financial assets of the Deposits Guarantee Fund amounted to 5,099,690 lats and net financial assets of the Fund for Protection of the Insured amounted to 656,279 lats.

Chairman of the Financial
and Capital Market Commission — Uldis Cērps

15 February 2002

BALANCE SHEET AS AT 31 DECEMBER 2001

(lats)

ASSETS	Note	31.12.2001.	01.07.2001. unaudited
ASSETS OF FUNDS			
LONG TERM INVESTMENTS		**-**	**-**
CURRENT ASSETS		**5,765,312**	**4,136,229**
Settlement of payables (receivables)		**669,746**	**3,938,606**
Due from State Budget to the Deposits Guarantee Fund		-	3,611,615
Due from State Budget to the Fund for Protection of the Insured		-	326,042
Due from market participants to funds	4	525,427	949
Other receivables	5	144,319	-
Investments in securities	6	**5,095,536**	**197,623**
Securities of the Deposits Guarantee Fund		4,484,062	-
Securities of the Fund for Protection of the Insured		611,474	197,623
Cash		**30**	**-**
TOTAL ASSETS OF FUNDS		**5,765,312**	**4,136,229**
ASSETS OF THE COMMISSION			
LONG TERM INVESTMENTS	3	**502,439**	**190,564**
Intangible assets		83,169	31,547
Fixed assets		331,547	159,017
Prepayments for long term investments		5,368	-
Leasehold improvements		82,355	-
CURRENT ASSETS		**893,132**	**414,051**
Stock		**7,419**	**9,918**
Accounts receivable		**148,828**	**207,005**
Due from State Budget for the State Insurance Supervision Inspectorate account balances in the State Treasury		-	160,779
Due from market participants	7	139,724	10,073
Settlement of other payables		1,000	26,913
Due from personnel		2,043	9,240
Overpaid taxes	8	6,061	-
Prepaid expenses	9	**361,828**	**1,312**
Cash		**375,057**	**195,816**
TOTAL ASSETS OF THE COMMISSION		**1,395,571**	**604,615**
TOTAL ASSETS		**7,160,883**	**4,740,844**

The accompanying notes on pages 37 to 42 form an integral part of these financial statements.

(lats)

LIABILITIES

	Note	31.12.2001.	01.07.2001. unaudited
LIABILITIES AND EQUITY OF FUNDS			
EQUITY	10	**5,755,969**	**4,136,229**
Net financial assets (budget result)		**5,755,969**	**4,136,229**
Net financial assets of the Deposits Guarantee Fund		5,099,690	3,611,615
Net financial assets of the Fund for Protection of the Insured		656,279	524,614
PAYABLES		**9,343**	**-**
Prepayments received in the Deposits Guarantee Fund		-	-
Prepayments received in the Fund for Protection of the Insured		9,343	-
TOTAL LIABILITIES AND EQUITY OF FUNDS		**5,765,312**	**4,136,229**
LIABILITIES AND EQUITY OF THE COMMISSION			
EQUITY	10	**1,350,244**	**602,042**
Net assets (budget result)		1,350,244	602,042
PAYABLES		**45,327**	**2,573**
Accounts payable to suppliers and contractors		29,656	2,065
Due to companies and personnel		-	94
Remuneration and withholdings (except taxes)		-	411
Taxes	8	6,485	-
Due to State Budget		-	3
Accrued income	11	9,186	-
TOTAL LIABILITIES AND EQUITY OF THE COMMISSION		**1,395,571**	**604,615**
TOTAL LIABILITIES		**7,160,883**	**4,740,844**

The accompanying notes on pages 37 to 42 form an integral part of these financial statements.

Chairman of the Financial and Capital Market Commission — Uldis Cērps

Head of Accounting Department — Rita Vanaga

15 February 2002

STATEMENT OF INCOME AND EXPENSES FROM 1 JULY 2001 TO 31 DECEMBER 2001

(lats)

INDICATORS	Note	Establishment and commencement budget	6 month budget	Total budget
REVENUES				
Payments of insurance companies		-	248,031	248,031
Life insurance companies		-	10,820	10,820
Other insurance companies		-	237,211	237,211
Bank of Latvia		688,299	600,000	1,288,299
State Budget		-	120,556	120,556
Other		-	(9)	(9)
Total revenues		**688,299**	**968,578**	**1,656,877**
EXPENSES				
Staff remuneration and other payments		(16,469)	(736,274)	(752,743)
Staff remuneration and other payments	12	(13,857)	(621,769)	(635,626)
Social security contribution		(2,612)	(114,505)	(117,117)
Staff insurance		-	(9,948)	(9,948)
Improvement of professional skills		-	(5,428)	(5,428)
Telecommunication and information		(1,269)	(21,145)	(22,414)
Public awareness and representation		(310)	(6,794)	(7,104)
Maintenance expenses		(87,113)	(36,636)	(123,749)
Rent		(66,666)	(3,134)	(69,800)
Public utilities		-	(6,003)	(6,003)
Maintenance of equipment		(4)	(342)	(346)
Materials and stationery		(1,347)	(11,644)	(12,991)
Business services		(1,200)	(8,890)	(10,090)
Insurance of property		-	(1,211)	(1,211)
Information technologies services		(4,738)	-	(4,738)
Other		(12,994)	(5,412)	(18,406)
Small items		(164)	-	(164)
Professional services		-	(7,811)	(7,811)
Business trips and participation in international organisations		-	(20,753)	(20,753)

STATEMENT OF INCOME AND EXPENSES FROM 1 JULY 2001 TO 31 DECEMBER 2001

(continued) (lats)

INDICATORS	Note	Establishment and commencement budget	6 month budget	Total budget
Depreciation/amortisation of capital investments		(44,067)	(17,825)	(61,892)
Software		(5,138)	(165)	(5,303)
Computers and data processing equipment		(10,946)	(12,621)	(23,567)
Furniture and fixings		(5,978)	(45)	(6,023)
Other fixed assets		(3,070)	(4,994)	(8,064)
Substantial repairs		(18,935)	-	(18,935)
Total expenses		**(149,228)**	**(862,614)**	**(1,011,842)**
Excess of revenues over expenses of the Commission		**539,071**	**105,964**	**645,035**
Excess of revenues over expenses of the Deposits Guarantee Fund and the Fund for Protection of the Insured	2	**-**	**1,164,303**	**1,164,303**
BUDGET RESULT		**539,071**	**1,270,267**	**1,809,338**

The accompanying notes on pages 37 to 42 form an integral part of these financial statements.

Chairman of the Financial and Capital Market Commission Uldis Cērps

Head of Accounting Department Rita Vanaga

15 February 2002

CASH FLOW STATEMENT
(FROM 1 JULY 2001 TO 31 DECEMBER 2001)

(lats)

INDICATORS	Note	Establish-ment and commence-ment budget	6 month budget	Total budget
RECEIPTS				
Payments of insurance companies		-	258,465	258,465
Life insurance companies		-	9,231	9,231
Other insurance companies		-	249,234	249,234
Payments of private pension funds		-	4,194	4,194
Bank of Latvia		688,299	600,000	1,288,299
State Budget		-	120,556	120,556
Cash transferred from State Treasury	13	-	160,628	160,628
Other		(280)	-	(280)
Total receipts		**688,019**	**1,143,843**	**1,831,862**
PAYMENTS				
Staff remuneration and other payments		(16,880)	(731,026)	(747,906)
Staff remuneration and other payments		(14,268)	(616,556)	(630,824)
Social security contribution		(2,612)	(114,470)	(117,082)
Staff insurance		-	(21,167)	(21,167)
Improvement of professional skills		(236)	(4,640)	(4,876)
Telecommunication and information		(2,345)	(21,221)	(23,566)
Public awareness and representation		(310)	(7,033)	(7,343)
Maintenance expenses		(436,890)	(29,183)	(466,073)
Rent		(410,499)	(3,134)	(413,633)
Public utilities		(226)	(2,017)	(2,243)
Maintenance of equipment		(126)	(342)	(468)
Materials and stationery		(1,367)	(11,124)	(12,491)
Business services		(832)	(5,533)	(6,365)
Insurance of property		-	(2,244)	(2,244)
Information technologies services		(4,738)	-	(4,738)
Other		(9,944)	(4,789)	(14,733)
Small items		(9,158)	-	(9,158)
Professional services		-	(4,252)	(4,252)
Business trips and participation in international organisations		(94)	(12,149)	(12,243)

CASH FLOW STATEMENT
(FROM 1 JULY 2001 TO 31 DECEMBER 2001)

(continued) (lats)

INDICATORS	Note	Establish-ment and commence-ment budget	6 month budget	Total budget
Capital investments		(365,195)	-	(365,195)
Software		(52,940)	-	(52,940)
Computers and data processing equipment		(98,999)	-	(98,999)
Furniture and fixings		(99,085)	-	(99,085)
Other fixed assets		(27,304)	-	(27,304)
Substantial repairs		(86,867)	-	(86,867)
Total payments		**(821,950)**	**(830,671)**	**(1,652,621)**
Net change in cash during the reporting period		**(133,931)**	**313,172**	**179,241**
Cash balance at the beginning of the reporting period	14	**195,816**	**-**	**195,816**
Cash balance at the end of the reporting period		**61,885**	**313,172**	**375,057**
Cash balance from the cash flows of Deposits Guarantee Fund and the Fund for Protection of the Insured	2	**-**	**30**	**30**
TOTAL CASH AT THE END OF PERIOD		**61,885**	**313,202**	**375,087**

The accompanying notes on pages 37 to 42 form an integral part of these financial statements.

Chairman of the Financial and Capital Market Commission — Uldis Cērps

Head of Accounting Department — Rita Vanaga

15 February 2002

STATEMENT OF CHANGES IN EQUITY (FROM 1 JULY 2001 TO 31 DECEMBER 2001)

(lats)

	Note	Result of Commission Establishment and Commencement budget	Result of Commission financing budget	Result of the Deposits Guarantee Fund	Result of the Fund for Protection of the Insured	Total
Budget result, 01.07.2001.	15	195,009	407,033	3,611,615	524,614	4,738,271
Changes relating to the previous period	16	5,182	97,985	421,249	34,188	558,604
Budget result of the reporting period		539,071	105,964	1,066,826	97,477	1,809,338
Budget result, 31.12.2001		**739,262**	**610,982**	**5,099,690**	**656,279**	**7,106,213**

The accompanying notes on pages 37 to 42 form an integral part of these financial statements.

Chairman of the Financial and Capital Market Commission — Uldis Cērps

Head of Accounting Department — Rita Vanaga

15 February 2002

NOTES TO THE FINANCIAL STATEMENTS

The Financial and Capital Market Commission (hereinafter – the Commission) was formed and acts in accordance with the Law on the Financial and Capital Market Commission. The Commission has acquired assets and liabilities of the Insurance Supervision Inspectorate, the Securities Market Commission and the Deposits Guarantee Fund Administration, as well as fixed assets granted by the Bank of Latvia.

The goal of the Commission's activities is to protect the interests of investors, depositors and the insured, and to promote the development and stability of the financial and capital market. The Commission is responsible for stability and development of the financial market.

1. Summary of significant accounting policies

Basis for preparation of the financial statements
The financial statements were prepared in accordance with the principles set in Instruction No. 1 issued by the State Treasury for the Preparation of Financial Statements.

Accounting principles applied
The financial statements were prepared in accordance with the following accounting principles:

- Accounting is performed on an accrual basis providing for recognition of revenue and expenses in the financial statements at the date of occurrence, irrespective of the related cash flows. Revenue is calculated on the basis of business activities performed by the participants of the financial and capital market, which are reported in the submitted financial statements, from which payments to be made are calculated.
- Assets are recognised at historic cost. Assets are booked on the date of acquisition at the amount of cash or cash equivalents, or at fair value of other consideration provided plus any other costs directly related to acquisition.
- Transactions and other undertakings are recognised taking into account their substance stating that transactions and undertakings should be recognised and disclosed according to their contents and economic substance and not only the legal form.
- The financial statements have been prepared on a going concern basis.

Fixed assets
Long term investments are recognised in accordance with the principles set by the Ministry of Finance in the Instructions for Accounting of State (Municipal) Budget Institutions and Municipal Budgets. Depreciation rates for long-term investments are applied in accordance with Regulation No. 96 on Depreciation Rates for Budget Institutions issued by the Cabinet of Ministers on 6 March 2001 which stipulates the following annual rates:

Computers and equipment	35%
Other fixed assets	20%

For fixed assets acquired from budget institutions for which the residual useful life is less than half of a useful life of a similar new asset, a 50% depreciation rate is applied.

Depreciation of fixed assets acquired prior to 31 December 2000 from the Insurance Supervision Inspectorate, the Securities Market Commission and the Deposit Guarantee Fund Administration was not charged to the Commission statement of income and expenses, instead the value of fixed assets and the result of Commission financing budget was decreased by the amount of depreciation. The depreciation rates for these assets were similar as applied to all other fixed assets. In the respective institutions fixed assets were expensed in their full value at the date of acquisition in the statement of income and expenses and a corresponding fixed asset fund for this amount was credited to equity.

If no depreciation was calculated on the fixed assets acquired from 1 January 2001 to 30 June 2001 it was recalculated in the reporting period from the date of acquisition and charged to the statement of income and expenses.

The following depreciation rates were applied to leasehold improvements:

Security systems	33%
Fixings	20%

Depreciation of fixed assets in the reporting period was charged to the statement of income and expenses.

Securities

Securities in the possession of the Commission are being held to maturity. Valuation of securities was performed using the straight-line discount amortisation method.

2. Cash flows, revenue and expenses of the Deposits Guarantee Fund and the Fund for Protection of the Insured

Cash flow and the actual result of revenues and expenses (in lats) of the Deposits Guarantee Fund and the Fund for Protection of the Insured from 1 July 2001 to 31 December was as follows:

	Cash flow	Revenues and expenses
REVENUES		
Payments to the Deposits Guarantee Fund	869,943	934,577
Payments to the Fund for Protection of the Insured	72,593	77,000
Payments of life insurance companies to the Fund for Protection of the Insured	9,060	11,801
Payments of other insurance companies to the Fund for Protection of the Insured	63,533	65,199
Income from investments	8,407	152,726
In the Deposits Guarantee Fund	2,529	132,248
In the Fund for Protection of the Insured	5,878	20,478
Transfer of cash from the State Treasury	3,937,657	-
Transfer to the Deposits Guarantee Fund	3,611,615	-
Transfer to the Fund for Protection of the Insured	326,042	-
Other payments	9,343	-
Total revenues	**4,897,943**	**1,164,303**
INVESTING ACTIVITIES		**-**
Investments in securities	**(5,266,024)**	**-**
Investing assets of the Deposits Guarantee Fund	(4,647,933)	-
Investing assets of the Fund for Protection of the Insured	(618,091)	-
Investments of the Fund for Protection of the Life Insured	(145,494)	-
Investments of the Fund for Protection of the Other Insured	(472,597)	-
Repayment of securities	**368,111**	**-**
Repayment of investments		

of the Deposits Guarantee Fund	163,871	-
Repayment of investments		
of the Fund for Protection of the Insured	204,240	-
Repayment of investments		
of the Fund for Protection of the Life Insured	79,989	-
Repayment of investments		
of the Fund for Protection of the Other Insured	124,251	-
Result of investing activities	**(4,897,913)**	**-**
RESULT	**30**	**1,164,303**

3. Long term investments

	Intangible assets	Fixed assets			Leasehold improve-ments	Pre-payments for long term investments	Total
	Licences and software	Computers and office equipment	Vehicles	Other			
Cost							
Book value 01.07.2001	**31,547**	**76,213**	**29,547**	**53,257**	**-**	**-**	**190,564**
Purchases	66,173	130,242	-	99,905	89,012	5,368	390,700
Write-offs and disposals	(4,982)	(4,303)	-	(927)	-	-	(10,212)
At 31.12.2001.	**92,738**	**202,152**	**29,547**	**152,235**	**89,012**	**5,368**	**571,052**
Depreciation/amortisation							
Charge	9,569	34,191	2,699	16,394	6,657	-	69,510
Depreciation of disposals	-	(897)	-	-	-	-	(897)
At 31.12.2001.	**9,569**	**33,294**	**2,699**	**16,394**	**6,657**	**-**	**68,613**
Book value 31.12.2001.	**83,169**	**168,858**	**26,848**	**135,841**	**82,355**	**5,368**	**502,439**

4. Due from market participants to funds

This item contains amounts due from financial and capital market participants to the Deposits Guarantee Fund and the Fund for Protection of the Insured for the quarter ended 31 December 2001.

	31.12.2001.	01.07.2001.
Due from market participants to the Deposits Guarantee Fund	485,883	-
Due from market participants to the Fund for Protection of the Life Insured	7,033	-
Due from market participants to the Fund for Protection of the Other Insured	32,511	949
	525,427	**949**

5. Other receivables

	31.12.2001.	01.07.2001.
Accrued income of the Deposits Guarantee Fund	129,719	-
Accrued income of the Fund for Protection of the Insured	14,600	-
	144,319	**-**

6. Investments in securities

This item contains purchased government securities disclosed at cost. During 2001, the Commission invested the cash of the Deposits Guarantee Fund and the Fund for the Protection of the Insured only in short term treasury bills issued by the Latvian Government. At the end of 2001, assets of the respective funds were invested in the following four issues of the Latvian Government securities:

Issue No	Purchase date	Maturity date	Discount rate (%)	Nominal value (lats)	Cost (lats)
LV0000531945	06.07.2001	04.01.2002	6.25	4,071,200	3,942,550
LV0000531960	05.10.2001	05.04.2002	5.50	212,100	206,204
LV0000531978	09.11.2001	10.05.2002	5.50	687,000	667,901
LV0000540664	20.07.2001	19.07.2002	6.69	299,100	278,881
					5,095,536

On 1 July 2001, the Commission acquired the securities portfolio of the Fund for Protection of the Insured in the amount of 197,623 lats. Respective Latvian treasury bills were redeemed during 2001.

7. Due from market participants

This item contains accounts due from financial and capital market participants as at 31 December 2001 to the Commission for the fourth quarter ended 31 December 2001. Outstanding receivables for financing of the Commission as at 1 July 2001 of 10,073 lats were settled in 2001.

8. Overpaid taxes

Type of tax	Balance at 01.07.2001	Calculated in 2001	Paid in 2001	Acquired tax liabilities	Balance at 31.12.2001
Social security contribution	-	157,494	(157,459)	(6,096)	(6,061)
Resident income tax	-	145,212	(139,642)	915	6,485
	-	**302,706**	**(297,101)**	**(5,181)**	**424**

Including:	**31.12.2001.**
Overpaid taxes	(6,061)
Tax liabilities	6,485

9. Prepaid expenses

	31.12.2001.	01.07.2001.
Prepayment for rent of premises until 9 January 2004	343,833	-
Staff health and accident insurance	14,997	1,259
Property insurance	1,339	44
Membership dues	1,186	-
Other	473	9
	361,828	**1,312**

10. Equity

This item contains net assets (budget result). Changes in net assets are disclosed in the Statement of Changes in Equity and Notes thereto.

11. Accrued income

This item contains advance payments made by private pension funds that will be credited to revenues of the Commission in future periods, as realised.

12. Staff remuneration and other payments

Contains remuneration to staff, including remuneration to the Council of 100,914 lats or 16% of total remuneration expenses.

13. Cash transferred from the State Treasury

Contains cash representing the balance of the Insurance Supervision Inspectorate in the State Treasury at 30 June 2001.

14. Cash balance at the beginning of the reporting period

Contains balance of the Commission's establishment and commencement of activities budget at 1 July 2001.

15. Budget result at 1 July 2001

Budget result of establishment of the Commission and commencement of its activities

Result of the Commission's establishment and commencement of its activities budget as at 1 July 2001 was 195,009, which was formed of the difference between State budget contribution (200,000 lats) and expenses (4,991 lats) until 1 July 2001.

Result of financing budget

Result of financing budget comprises net assets acquired by the Commission from the following institutions:

Bank of Latvia	43,894
Insurance Supervision Inspectorate	299,616
Securities Market Commission	55,710
Deposits Guarantee Fund Administration	7,813
	407,033

Budget Result of the Deposits Guarantee Fund and the Fund for Protection of the Insured

This item contains total net assets acquired from the Deposits Guarantee Fund and the Fund for Protection of the Insured (budget result of the previous period).

16. Changes relating to the previous period

Until 1 July 2001, certain items were accounted on the cash flow basis. The following changes relating to the previous period were made to ensure compliance with the principle of accruals.

Changes to budget result of the Commission establishment and commencement of its activities

This item contains changes to the result of the Commission's establishment and commencement of activities budget: tax surplus of the acquired institutions (refer to Note 8), which was added to the Commission's establishment and commencement of activities budget.

Changes to budget result of the Commission's financing budget

This item contains changes to the budget result for the previous period – payments of insurance companies for financing the Commission in the quarter ended 30 June 2001, the value of disposed fixed assets and equipment of the acquired institutions and the calculated depreciation of the fixed assets acquired from the budget institutions.

Changes to budget result of the Deposits Guarantee Fund and the Fund for Protection of the Insured

This item contains changes to the budget result for the previous period – payments of the financial and capital market participants to the Deposits Guarantee Fund and the Fund for Protection of the Insured for the quarter ended 30 June 2001.

17. Significant agreements

On 5 December 2000 an agreement was concluded with SIA "Drave" on the rent of premises at Kungu iela 1, Riga for 10 years. The agreement was renewed on 2 August 2001.

KPMG

AUDITORS' REPORT
TO THE PARLIAMENT OF THE REPUBLIC OF LATVIA

We have audited the accompanying balance sheet of the Financial and Capital Market Commission as at 31 December 2001 and the related statements of income and expenses and cash flows for the period from 1 July 2001 to 31 December 2001, as set out on pages 30 to 42. The financial statements are the responsibility of the Management of the Financial and Capital Market Commission. Our responsibility is to express an opinion on the financial statements based on our audit.

We conducted our audit in accordance with International Standards on Auditing as issued by the International Federation of Accountants. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements present a true and fair view on the financial position of the Financial and Capital Market Commission as at 31 December 2001, as well as its statements of income and expenses and cash flows for the period from 1 July 2001 to 31 December 2001, in accordance with the accounting policies of the State Treasury instructions of the Republic of Latvia as adopted by the Financial and Capital Market Commission.

KPMG

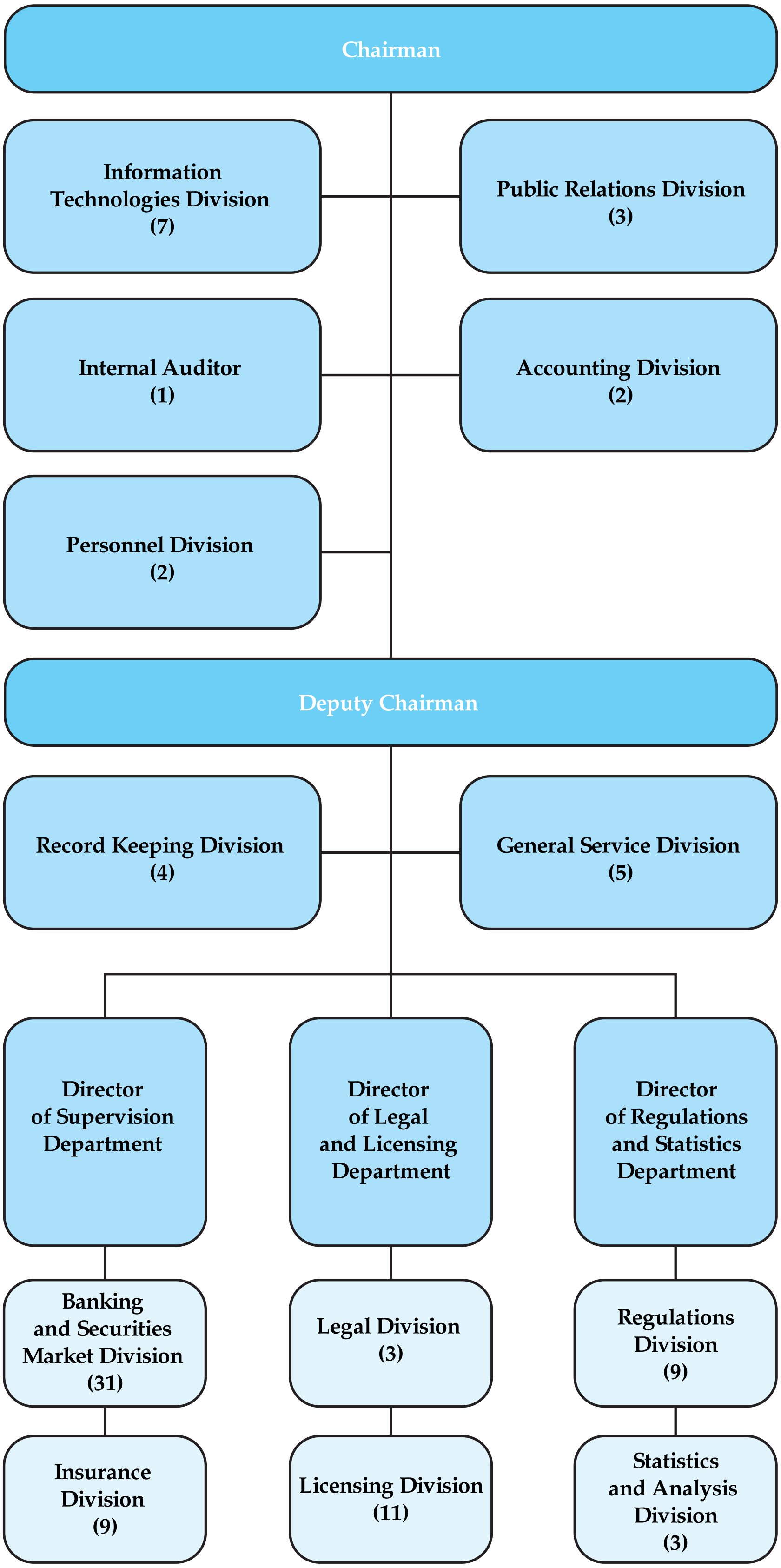
KPMG Latvia SIA
Riga, Latvia
15 February 2002

Užāne

Valda Užāne
Sworn Auditor
personal code 030259-11286
Certificate No. 4

Annex

STRUCTURE OF THE FINANCIAL AND CAPITAL MARKET COMMISSION



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