FINANŠU UN KAPITĀLA TIRGUS KOMISIJA

ANNUAL REPORT OF THE FINANCIAL AND CAPITAL MARKET COMMISSION OF THE REPUBLIC OF LATVIA FOR 2007

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List of Abbreviations

Commission – Financial and Capital Market Commission
Consultative Council – Consultative Council of the Financial and Capital Market
CSRI – Central Storage of Regulated Information
DGF - Deposit Guarantee Fund
EEA – European Economic Area
EU – European Union
FPI – Fund for the Protection of the Insured
LCD – Latvian Central Depository
RSE – Riga Stock Exchange
Saeima - Latvian parliament
SFPS – State-funded Pension Scheme

Introduction. Latvia's Economy and Financial Markets in 2007

Irena Krumane
Chairwoman
Financial and Capital Market Commission

To ensure macroeconomic stability in such a small country in terms of size as Latvia is, the sound banking system subject to professional supervision is a rather important prerequisite. Efficient risk management and profit making are at the heart of the banking system while the supervisory authority must follow the processes accurately – which risks are growing and which are expected to appear in the future.

The banking credit risk has been constantly growing in Latvia since 2000, when loans comprised just 25% of bank assets, but at the end of 2007 loans amounted to 68% of total bank assets. Lending has developed in Latvia starting from a very low baseline; thus the rapid year-on-year growth rate (in 2007 - 37%, in 2006 - 56%) is due to the very low initial position. Over this period financial services have grown into an integral component of everyday life of Latvian people. According to the sociological and market research data (the leading centre of market and sociological researches SKDS performs an annual survey commissioned by the Financial and Capital Market Commission), in 2007 already 80% of Latvia's residents trusted banks, while in 2007 – this ratio was 75%. A similar growth in customer trust was observed in the insurance business – 69% of residents trusted insurance companies in 2006, but in 2007 – 74%, and customer trust has increased also in other segments of the financial and capital market in 2007.

In 2007, there were 153 000 households which had taken housing loans. About one half of real estate transactions in Latvia had been carried out without taking loans. In Latvia, the real estate and lending market saturation, which is typical of the average figures of European markets, has been reached in about four years, and it could be regarded as a very high rate.

The gross domestic product (GDP) growth of late years (in 2007 it was 10.3%) indicates an upward phase of economic development and that Latvia's economy has been among most rapidly developing global economies in last eight years. An essential impetus to the above growth, of course, was an increase in mortgage lending that, in turn, was boosted by the increasing resident purchasing power and demand for higher living standard.

Since the economy has been developing cyclically, a new stage began in the second half of 2007, which could be regarded as the economic development slowdown in comparison to the previous period. It has made an impact also on the banking sector; namely, crediting rate has fallen from 54% on average over three past years to 37% in 2007. The anti-inflation action plan for slowing down the economic growth, introduced by the government in mid-year, can be mentioned as one of material factors, for example, a 10-percent initial downpayment requirement on the mortgage credit. But in the current phase of economic slowdown it is important to find a balance between the inflation mitigation measures and the measures to boost economic activity. Whereas the requirement for the notification from the State Revenue Service (also a constituent part of the above plan) regarding the borrower's legal income will still be a prerequisite in the future, to ensure that banks receive true and equitable information on the borrower's income.

Most believably, in the future there will be no such steep economic growth as up to now – an average 10-percent increase in GDP over a three-year period. The current economic phase compels people to think over their savings, as the users of the Latvian financial services take out numerous loans but make insignificant savings for the time being. Whereas those financial market participants whose business is provision of savings service (endowment insurance, insurance unit links, investments in funds), are just at the very outset of their growth. Insurance gross premiums written accounted for 142 lats per resident in 2007 (in 2006 – 90 lats), thus making almost a 60-percent increase in 2007. Evidence of this is also the rise in foreign investments in insurance business over past two years as well as foreign insurers' competition in the Latvian market.

Considering from a viewpoint of risk management, a topical question in the reporting year concerned the possible decrease in borrowers' income or losing their job. According to statistics, those residents who had taken loans from the Latvian banks generally would be capable of repaying the loans. In 2007, only 0.5% of total banking credit portfolio comprised provisions for non-performing loans. In the future, the figure could grow up to 1%–2%, but the Latvian financial institutions have made themselves ready for that. Capital adequacy ratio of the Latvian banks still remains high; by the end of 2007 it was 11% (EU Directives require a minimum capital ratio of 8%). This means that the Latvian banks have sufficient provisions to overcome possible losses.

Latvia's membership in the European Union and participation in the global financial markets have brought new opportunities and challenges to our financial market, for instance, the market turmoil in 2007 resulting from the US mortgage market crisis. Therefore for the purpose to become an efficient and dynamic supervisory institution that ensures high standards in the financial service area and promotes the financial and capital market development in Latvia, in 2008 the Financial and Capital Market Commission has decided to develop a new strategy for the period from 2009 to 2011. Besides, more attention will be paid to analytical work, which encompasses studying credit risk and liquidity risk in the banking sector and a month-on-month analysis of the overall system.

In the reporting year, an analysis was already carried out to compare obligations of the Latvian banks arising from the national rules in the area of anti-money laundering with the relevant requirements of the US legislation. It is also planned to develop a conceptual solution for the classification of activity models of the Latvian bank customers, non-residents, thus allowing for a better assessment of risks arising from activities of such customers.

Preparing analytical information and providing explanation on a regular basis will boost a dialogue between the local market participants and international financial market as well as provide instructions and information for the Latvian residents about key tendencies and service reliability. Transposition of the requirements of EU directives into the national law will be also continued making a number of amendments to the Latvian legislation and developing new regulations of the Financial and Capital Market Commission.

I truly hope that zealous and diligent teamwork in line with the financial sector will help us to accomplish the tasks in order to take on new challenges in the future!

Chairwoman
Financial and Capital Market Commission

Irena Krumane

Report of the Board of the Financial and Capital Market Commission

The Financial and Capital Market Commission (the Commission) carries out supervision over banks, credit unions, insurance undertakings and insurance brokers, participants of financial instruments market as well as private pension funds in accordance with the Law on the Financial and Capital Market Commission.

The Commission has been operating as an entirely autonomous public institution since commencing its activity on 1 July 2001. The Commission was governed by the Board membership of which remained unchanged since its approval till the end of the reporting year and was as follows: Chairman – Uldis Cērps, Deputy Chairman – Jānis Brazovskis, Board members – Ludmila Vojevoda, Jānis Placis and Gvido Romeiko.

In 2007, for the first time the activities of the Commission were financed solely by payments from the participants of financial and capital market. Until the year 2007, financing for the Commission's activities was provided also by payments from the national State budget and from the Bank of Latvia. In 2007, the Commission did not provide any paid services and did not receive any donations.

In 2007, the Board of the Commission held 52 meetings and adopted 188 decisions. Of total, 33 decisions were binding on all of the financial and capital market participants, but 130 decisions applied to individual market participants, of which 27 were unfavourable but 103 decisions were favourable to them. Whereas 25 decisions were made regarding the management of the Commission's own activities.

In 2007, the Consultative Council of the Financial and Capital Market (the Consultative Council) held 12 meetings where draft legislation binding on the financial and capital market was considered. The Consultative Council was also notified on a regular basis of contributions made into the Deposit Guarantee Fund and the Fund for the Protection of the Insured, as well as of the management of assets of the funds. The Consultative Council assessed and supported both the Commission's draft budget for 2008 and the operations plan for 2008.

In the reporting year, 14 amendments to 12 laws, six new regulations issued by the Commission and nine regulatory amendments were drafted and took effect. To introduce the principle of one-stop-agency in order to facilitate the procedure of submission of annual reports to the public authorities for banks, financial institutions and insurance companies, the Commission experts drafted amendments to the Law on the Financial Instruments Market, Law on Investment Management Companies, Credit Institution Law, Credit Union Law, Law on Insurance Companies and Supervision Thereof, as well as the Law on Private Pension Funds.

During the reporting year, the Commission continued maintaining and enhancing its Quality Management System pursuant to ISO 9001:2000 standards. The Commission's internal control system operated effectively and in 2007 audit inspections were conducted by internal audit and SIA Bureau Veritas Latvia, both attesting conformity of the Commission's Quality Management System to ISO 9001:2000 standards.

In 2007, the Commission conducted a survey of the Commission's customers. According to the results of the survey, a majority of the market participants (customers) were satisfied with the activities of the Commission. Using the five-point grading system, overall assessment of the Commission's work was 4.5 points. Whereas recommendations made by the respondents were summarized and discussed at a quality management review meeting to improve the Commission's operations in 2008.

At the end of 2007, the number of employees at the Commission was 95. The Commission's specialists attended seminars to perfect their knowledge regarding credit risk management systems in commercial banks, new capital requirements for banks or Basel Capital Accord II and other relevant financial supervision matters, as well as regarding anti-money laundering measures and counter terrorism financing (AML/CTF) measures.

The budget for the year 2008 and the operations plan for 2008 approved by the Commission are available on the Commission's website at www.fktk.lv.

Licensing

	BEGINNING OF 2007	END OF 2007	NEW MARKET PARTICIPANTS
Banks	21	21	0
Branches of foreign banks	3	4	2
Cooperative credit unions	35	35	0
Banking service providers from EEA	122	181	61
Insurance companies	16	15	-
Branches of foreign insurers	5	7	2
Insurance service providers from EEA	264	319	64
Investment management companies	13	14	1
Investment management service providers from EEA	4	11	7
Investment firms	6	7	1
Investment brokerage service providers from EEA	276	628	358
Private pension funds	6	6	0
Insurance brokerage companies	45	69	24
Insurance agents	626	713	93

Issuers

At the close of the reporting year, 53 issuers had their prospectuses registered in Latvia or permissions issued to make offerings in Latvia. In 2007, on the basis of a single licence principle, issuers from the European Union (EU) member states commenced issuing of their financial instruments on the Latvian market; in total 12 notifications of intent of issuing financial instruments were received from the issuers of the EU member states.

In the reporting year, 13 issues of various securities were performed in Latvia. Among the public offerings made by the issuers whose prospectuses were registered in Latvia or having permission to make a public offering, debt securities issued by the Latvian banks prevailed, i.e. bonds (2) and mortgage bonds (5), as well as a short-term bond (1). Two base prospectuses were registered entitling the issuer to perform one or several issues of transferable securities (except capital securities) in a fixed period of time.

In 2007	Number
Prospectuses registered	**1 – regarding admitting shares to trading on a regulated market**
	2 – regarding admitting bonds to trading on a regulated market
	3 – regarding admitting of mortgage bonds to trading on a regulated market
IN TOTAL	**6**
Public offerings issued	**3 – regarding admitting shares to trading on a regulated market**
	1 – public offering of shares without admitting to trading on a regulated market
	3 – regarding debt securities of companies
IN TOTAL	**7**
Share buyout offers made	**5 mandatory share buyout offers**
	3 final share buyout offers
	1 mandatory and final share buyout offer on a consolidated basis
IN TOTAL	**9**

Supervision

In 2007 the supervision of the financial sector was grounded in assessing operational risks incurred by market participants on the basis of financial account analysis. Such analysis allows for evaluating the financial stability of market participants, operational risks and their trends, and the conformity of participants' operations with the requirements specified by the law. The results of this analysis were regularly submitted to the Board of the Commission, which then discussed the future tasks and priorities of supervision. The analysis of financial reports was also used to plan on-site inspections. The primary purpose of such inspections was to evaluate the financial stability of the institution under supervision, to assess its capital adequacy and to examine whether an internal control system of the institution ensures that risks are adequately monitored and managed. By revealing the causes of arising problems timely and finding solutions to them, the possibility of failing to fulfil obligations by an individual market participant has been reduced, as well as the possible influence of such problems on the financial and capital market as a whole. All banks were notified of main trends and deficiencies detected during inspections by the statements of the Commission.

Supervision of Banks

In the reporting year, 21 banks and four branches of foreign banks operated in Latvia. During the reporting year, the Commission conducted 23 bank inspections, in particular focusing on lending as well as risk management, namely - operational risk, interest rate risk, foreign exchange risk, liquidity risk.

The underlying document for carrying out bank inspections is the Commission's Bank Risk Assessment Manual which sets out the core principles for identifying risks incurred by activities of institutions subject to supervision as well as for analysis and assessment of quality, adequacy and compliance of approaches used to the size and complexity of activities.

Taking into account the principles laid down in the Bank Risk Assessment Manual, planning bank inspections and using information available from financial reporting and internal control management information, assessment of banks is carried out with a purpose to determine material business units/areas and business activities in each material business group's company where attention should be paid during the inspection. A decision on whether business units/areas and business activities in each business group company are regarded as material is made using qualitative and quantitative criteria in accordance with methodology. The Commission identifies the risks and the aspects of risk management for each unit, which is to be assessed. At the end of 2007, overall 10 banks had undergone the assessment pursuant to the above methodology. Results of assessment allow the Commission to compare assessments of bank activities and use them in planning further inspections.

Lending

Upon the significant growth in the amount of loans issued by banks, 16 inspections were conducted in the reporting year during which time the Commission's specialists examined the quality of credit portfolio and the banks' credit risk management systems (identification, measuring, supervision and control of credit risk) in order to timely identify any weaknesses and possible credit repayment problems. The strategies, policies and procedures for granting credits and their implementation were evaluated.

The banks were mostly admonished for deficiencies in assessing creditworthiness of individuals that, in the Commission's view, may increase risks related to housing crediting for individuals. The Commission proposed and monitored the measures to be taken to eliminate above shortcomings. Overall, the housing credit portfolio quality and credit risk management were assed as satisfactory and no additional provisions were required.

In view of the specific weight of credit portfolio in the banking assets and considerable increase in the banking assets, special attention was paid to management of concentration risk in credit portfolios of banks and procedures for stress testing. In 2007, the Commission issued a fine of 1 000 lats to one bank for violation of regulatory requirements regarding credit risk management.

Pursuant to the plans of two Latvian banks to apply the internal ratings based approach to determine credit risk capital requirements, inspections were performed in 2007 with an intent to assess the quality and course of implementation of this approach.

Risk management function

Providing financial services, banks must ensure not only efficiency of each business unit or business activity, but also the development and efficient implementation of an integrated risk management function relevant for activities of banks. When performing nine bank inspections in 2007, the Commission paid greater attention to the quality of operational risk, interest rate risk, foreign exchange risk, liquidity risk and strategic risk management.

As part of assessment of each integrated risk management function, the size of respective risk and impact of changes on the activities of bank at large were evaluated, as well as efficiency of internal control system and management functions in identifying, measuring and monitoring respective risks. In particular, the Commission analyzed whether the banks had used results of various scenarios and stress testing procedures in risk management.

Compliance function

According to the Commission's Regulations on Establishing an Internal Control System adopted on 2 May 2007, banks must establish an internal control system taking into account the size of the institution, the amount, nature and complexity of the activities of the institution, as well as risks regarding each business line, the stage of management centralization, information technologies and other factors which are material for the implementation of objectives of the respective institution. The internal control system must cover policies and control procedures determined by the bank management in order to manage risks related to the bank's activities.

In assessing the compliance function, the Commission evaluated efficiency of bank internal control system and corporate management overall. An emphasis was laid to make certain whether the internal control systems developed by the banks ensured compliance with law provisions and allowed for duly compliance with the changes in legal norms regarding the spheres linked to the banking activities, incl. foreign countries where the banks performed their activities.

Compliance function covers also the risk of laundering of proceeds derived from criminal activity and terrorism financing, namely, compliance function may be insufficient to ensure observance of the provisions of the anti-money laundering and terrorism financing laws, incl. the risk that the bank could be involved in laundering of proceeds derived from criminal activity and financing of terrorism.

Assessing the above risk, in 2007 the Commission continued paying attention to activities of the market participants so that they would observe the Know Your Client (KYC) principle and be able to ensure the timely identification of unusual and suspicious transactions and report to the Office for the Prevention of the Legalization of Proceeds Derived from Criminal Activity of them as well as the market participants be able to refrain from execution of such transactions.

Besides, the Commission paid attention how the market participants observed the provisions of Regulations for the Formulation of an Internal Control System for the Prevention of Laundering of Proceeds Derived from Criminal Activity and Financing of Terrorism passed in 2006.

In 2007, the Commission conducted 15 inspections to probe the banks' compliance with the provisions of the Law on the Prevention of the Laundering of Proceeds Derived from Criminal Activity and to evaluate the quality and effectiveness of the banks' internal control systems. The Commission fined five banks in the amount of 40 000 lats for drawbacks in the internal control system due to which inadequate monitoring of the clients' economic activities was detected.

While carrying out inspections in 2007, material improvements in quality and efficiency of the banks' internal control systems for the prevention of laundering of proceeds derived from criminal activity were observed. Pursuing a practice of previous years, in 2007 the Commission aggregated the cases having the typology of unusual and suspicious transactions and provided all the market participants with this information thus ensuring that the internal control systems would be capable of ensuring timely identification of suspicious transactions.

Within anti-money laundering framework, in 2007 the Commission's specialists took part in work of Committee on the Prevention of Money Laundering and Terrorist Financing of the European Commission, as well as in the joint 3L3 Task Force on AML/CTF including the members of three European Union committees (Committee of European Banking Supervisors (CEBS), Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) and Committee of European Securities Regulators (CESR)).

In 2007, the Commission's specialists continued their participation in work of the Selected Committee of Experts on the Evaluation of Anti-Money Laundering Measures (MONEYVAL). The progress report of Latvia on the implementation of the IMF Report on Latvia's observance of FATF recommendations for anti-money laundering and combating the financing of terrorism was reviewed and approved at the MONEYVAL's 25th plenary meeting.

In 2007, the Commission started drafting the new Law on the Prevention of Laundering the Proceeds from Criminal Activities and Terrorist Financing to transpose the provisions of Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing and the Commission Directive 2006/70/EC of 1 August 2006 laying down implementing measures for Directive 2005/60/EC of the European Parliament and of the Council as regards the definition of the term "politically exposed person" and the technical criteria for simplified customer due diligence procedures and for exemption on grounds of a financial activity conducted on an occasional or very limited basis. Following lengthy discussions with financial and capital market participants, the draft law was finalized and on 17 August 2007 it was submitted to the Ministry of Finance with a request to promulgate it at the meeting of state secretaries. Upon coordination of the law between the ministries and relevant public institutions, the draft law was reviewed at the meeting of the Cabinet of Ministers on 11 December 2007, and submitted to Saeima on 18 December 2007.

Supervision of cooperative credit unions

In the reporting year, there were 35 cooperative credit unions operating in Latvia, where the Commission conducted three inspections. The probes sought to assess loan portfolio of credit unions and compliance with provisions of regulatory norms regarding the lending sector. Considering the deficiencies established the Commission determined and controlled measures to be taken for the prevention of the above deficiencies.

Supervision of financial instruments market

In supervising the operation of the financial instruments market, the Commission paid particular attention to:
- detecting market manipulation,
- setting up and maintaining the lists of inside information holders by the public joint stock companies, notifications of persons listed in the inside information holders' lists pursuant to the law and detecting insider dealings,
- disclosing significant events timely, incl. financial information on the activities of public joint stock companies;
- providing information about acquiring or losing qualifying holdings in public joint stock companies.

The Commission constantly monitored the regulated market to ascertain that no market manipulations were taking place. For this purpose, since 2005 the Commission has been making use of information provided by the Riga Stock Exchange (RSE) on a regular basis regarding the orders submitted to the RSE and the completed orders with financial instruments listed in the regulated markets, as well as providing information on inside information bearers of issuers. Until the end of 2007, the RSE maintained the list of holders of inside information according to information provided by issuers and made available the list to all banks and investment brokerage firms so that they were able thereby to monitor transactions carried out by their customers, the holders of inside information. At the close of 2007 pursuant to the changes in regulatory norms, the Commission took over responsibility for the maintenance of the list of holders of inside information from the RSE and therefore in 2007 the Commission created a new database. By the end of the reporting year there were about 2.6 thousand inside information bearers in Latvia.

Pursuant to Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments, requirements for information exchange on transactions in financial instruments between the EU supervisory authorities, in 2007 the Commission developed a new information system to ensure that competent authorities of relevant countries also receive information on transactions in financial instruments admitted to trading on the regulated markets of European Economic Area (EEA) performed by Latvia-registered investment firms and credit institutions providing investment services. The Commission receives information also about transactions in financial instruments admitted to trading on the regulated market of the Republic of Latvia performed by the EEA-registered investment firms and credit institutions. The new information exchange procedure essentially improves and facilitates information receipt and efficient supervision of transactions in financial instruments admitted to the regulated markets.

In 2007, pursuant to the requirements of Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market the Commission worked out a new information system – the Central Storage of Regulated Information. The objective of the Central Storage of Regulated Information is to provide a joint system for storing all the information that issuers whose financial instruments are admitted to trading on the regulated markets of the Republic of Latvia must disclose to the public. In accordance with the provisions of the Law on the Financial Instruments Market the issuers whose financial instruments are admitted to trading on the regulated markets of the Republic of Latvia will have to at first disclose all the information to the Central Storage of Regulated Information and only after that to other mass media. The Central Storage of Regulated Information has opened its own website at www.oricgs.lv.

In 2007, the Commission implemented two administrative proceedings regarding possible insider dealings, and having observed several indications implying the fact that market operations of an investor could have been carried out using inside information regarding activities of an issuer, required an assessment of the law enforcement institutions on whether any constituent elements of a criminal offence were spotted.

In 2007, when probing whether the issuers whose financial instruments are admitted to trading on the regulated markets had observed the provisions of the Law on the Financial Instruments Market regarding establishment and maintenance of the list of inside information holders and notifying RSE, the Commission detected violations and in four cases issued relevant administrative acts, giving a warning.

In 2007, while checking whether the persons included in the list of inside information bearers had observed the requirement of the Law on the Financial Instruments Market regarding information disclosure during the reporting year regarding notifying the RSE of transactions performed, the Commission detected violations and in eight cases issued relevant administrative acts, imposing a fine of 1 000 lats per person on two persons but six persons received a warning.

In accordance with requirements of the Law on the Financial Instruments Market, the issuer whose financial instruments are admitted to trading on a regulated market must notify the organizer of the regulated market of significant events, incl. disclosure of financial information. In 2007, the Commission performed 22 inspections aiming to verify whether issuers disclose information on significant events fully and timely to the Central Storage of Regulated Information, created by the Commission. Upon detecting violations, in nine cases the Commission demanded the issuers to take measures depending on the offence to ensure the information be disclosed timely in the future and initiated eight administrative proceedings on non-disclosure of information regarding issuer's significant events, and as a result relevant administrative acts were issued, imposing a fine of 1 000 lats per person on three persons, and three persons received a warning, but in two instances the inspection is still continuing and a decision would be taken in 2008. Non-disclosure of significant events was mostly related to failure to timely submit financial reports on performance and forecast of the issuers.

In accordance with requirements of the Law on the Financial Instruments Market, the issuer whose financial instruments are admitted to trading on a regulated market must observe the requirements for disclosure of financial reports. In 2007, the Commission conducted nine examinations to verify whether the issuers in disclosing their financial reports had complied with the provisions of the Law on the Financial Instruments Market. In all cases where deficiencies were detected, the Commission ordered the issuers to remedy the situation.

In 11 instances, the Commission conducted inspections on the basis of facts at its disposal implying that a person had not notified about the acquisition of a qualifying holding in the issuer's voting capital or failed to notify of selling shares or losing a holding in the amount as prescribed by the Law on the Financial Instruments Market. In seven administrative procedures in 2007, unfavourable rulings were issued to market participants and a warning given for a failure to notify of changes in a qualifying holding. A fine of 5 000 lats was imposed on a person who had acquired shares in the amount above 50 percent of the issuer's voting capital but failed to make a mandatory share buyout offering.

Inspections of two banks – issuers of mortgage bonds - were performed in 2007. Detecting drawbacks in keeping the Mortgage Bond Cover Register or the list of inside information holders, the Commission applied and monitored measures taken to prevent deficiencies.

Supervision of investment firms and investment management companies

At the end of the reporting year, there were 13 investment management companies and six investment firms operating in Latvia. Twenty Latvia-registered banks and one foreign bank branch also offered investment services. On 31 December 2007, 99.7% of all client investments in financial instruments were carried out via banks.

The on-site inspections at one investment management company and at five banks – investment brokerage service providers were conducted in 2007. When ascertaining that complete and precise information regarding provision of brokerage services is not always provided to customers, the Commission ordered investment brokerage service providers to carry out improvement actions. In performing inspections, the Commission also evaluated the quality and efficiency of methodology for identification of manipulative transactions and preventive procedures developed by investment brokerage service providers. Taking account of detected shortcomings in the above procedures, the Commission determined and monitored measures be taken for improvement of internal regulations of investment brokerage service providers and their implementation.

At the close of 2007, a licence for management of State-funded pension scheme (SFPS) assets was issued to nine investment management companies. Supervision of SFPS private asset managers was carried out on the basis of receiving and analyzing financial reports. In the reporting year, a new supplemented reporting system was introduced for SFPS asset managers allowing the Commission to receive more detailed information to make certain whether SFPS asset investments met the restrictions set by the law. Simultaneously, the amount of monthly reports to be submitted to the Commission was reduced thus easing administrative burden of the SFPS private asset managers.

Supervision of the organizer of regulated market (RSE) and Latvian Central Depository

In carrying out its functions under the supervision, the Commission assessed the compliance of the regulations drafted by the Central Depository and RSE with the provisions of the Law on the Financial Instruments Market and other normative acts, and an effective performance of their obligations. In 2007, the Commission considered draft amendments to two regulations issued by the Central Depository and one regulation issued by RSE and did not object to their approval.

Supervision of private pension funds

At the close of 2007, there were six private pension funds operating in Latvia. In the reporting year, an on-site inspection of one private pension fund was conducted. The examination sought to assess compliance of the calculation of the accrued additional pension capital of the pension plan participants with legal norms.

In the reporting year, a new reporting system was introduced for the private pension plans pursuant to amendments to the law.

Supervision of insurance companies

At the end of 2007, 11 non-life insurance companies and four life assurance companies operated in Latvia.

A two-stage supervisory process has been exercised over the insurance companies; the Commission analyzes reports of the insurance companies evaluating the compliance of the activities of insurance companies with provisions of the law. The Commission scrutinizes the performance of the insurance companies and new trends in their results on a regular basis, and where appropriate issues specific instructions and measures for remedying deficiencies.

In 2007, the Commission conducted five full-scope inspections of the activities of insurance undertakings, including three inspections of life insurance undertakings and two inspections of non-life insurance companies. In these inspections, special attention was paid to the assessment of adequacy of the assets of the insurance companies and their technical provisions to insurance and accepted reinsurance contracts, as well as transfer of reinsurance liabilities, assessment of compliance of technical provisions adequacy and technical provisions investments with the provisions of the Law on Insurance Companies and Supervision Thereof, and compliance of the internal control systems in place at the insurance companies with the provisions of the Law on the Prevention of the Laundering of Proceeds Derived from Criminal Activity. The Commission issued instructions for eliminating shortcomings discovered during the inspections. During the examinations, internal control systems were evaluated, to make certain that insurance companies were aware of possible risks. Risk assessment of each insurance company was drawn up after the inspections, which was then reviewed at the Commission's Board meeting. Risks related to risk underwriting, accrual of technical provisions, liabilities reinsurance, making investments, as well as management risk, operational risk and reputation risk were assessed in the assessment of risks.

During inspections at the insurance companies in 2007, the Commission detected no such failures to observe regulatory norms that require imposing sanctions or fines as prescribed in the Law on Insurance Companies and Supervision Thereof.

Additional Supervision

In 2007, the Commission performed additional supervision of Latvia-registered and authorized insurance company in accordance with the provisions of the Law on Insurance Companies and Supervision Thereof. The Commission analyzed reports of the insurance company subject to additional supervision regarding the adjusted required solvency margin and adjusted available solvency margin and report on intra-group transactions of insurance group as well as collaborated with supervisory authorities of relevant Member States.

In 2007, the Commission cooperated with insurance supervision authorities of Member States that perform additional supervision pursuant to requirements of regulatory norms providing information on operational risks and ability to fulfil obligations of insurance group companies, which are registered and authorized in the Republic of Latvia.

Guarantee fund for the compulsory third party liability insurance for owners of inland motor vehicle

Pursuant to Section 51 of Compulsory Civil Liability Insurance of Owners of Motor Vehicles Law and Clause 19 of the Cabinet of Ministers Regulations No 195 regarding the Procedure of Establishment, Accrual and Administration of the Guarantee Fund for the Compulsory Third Party Liability Insurance for Owners of Inland Motor Vehicles, in 2007 the Commission conducted an inspection of the guarantee fund administered by the Motor Insurers' Bureau of Latvia regarding of the procedure of establishment, accrual and management and informed the Ministry of Finance and the Motor Insurers' Bureau about the results of the control of the guarantee fund.

Supervision of Information Systems

Under its supervision functions, the Commission carried out both full-scope inspections and inspections of critical security of information systems of market participants in the reporting year. To ensure efficiency of security audits for information systems conducted by the Commission, the audit methods based on both the compliance audit and the risk assessment audit techniques were applied.

In 2007, the Commission started assessing of the bank readiness to use internal model approaches for the calculation of capital requirement for credit risk and operational risk in view of information security systems.

During these inspections, the Commission focused on verifying the priorities as follows:
- whether a market participant has developed and applies in practice rules for organization information system security;
- whether a market participant has implemented an independent and efficient security control function for its information system;
- whether a market participant carries out planning, documenting and testing of business continuity.

Information acquired during inspections allows for drawing conclusions that arrangements and management of market participant security are still at different development stages but in view of potential IT risks the market participants, at large, have been paying an increasing attention to the information system security and investing more resources in it. Following the inspections, the market participants coordinated the plan and schedule for eliminating deficiencies with the Commission and its implementation is under supervision.

Review of Client Complaints

The specialists of the Commission in the reporting year examined client complaints and comments regarding the participants of Latvia's financial and capital market. In 2007, in total 220 submissions were examined, incl. 101 concerned operations of credit institutions, 89 – insurance business, 15 - financial instruments market participants, two - management of State-funded pension scheme assets, one – the Commission's employees, and 12 general submissions.

Though in the majority of cases the Commission did not have the legal right to resolve civil disputes between market participants and their clients, as such cases are to be mediated in courts of law, the Commission's specialists considered complaints and required additional information from the market participants involved. This helped the Commission to determine whether the market participant had not violated any laws or regulations falling within the competence of the Commission. In cases when the complaints did not fall within its competence, the Commission pursuant to the Law on Procedures for Examining Applications, Complaints and Proposals in State and Municipal Authorities requested other competent institutions to examine the above complaints or provide information to the submitter that such case is to be mediated in the court.

Operation of Guarantee Funds

Deposit Guarantee Fund

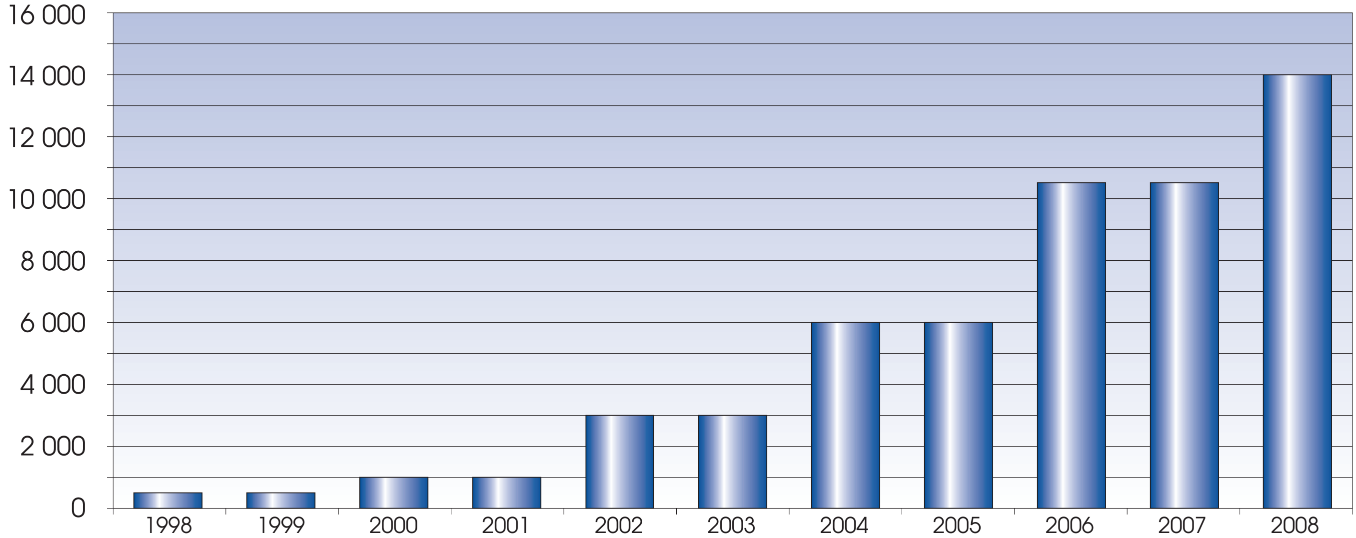
In 2007, the guaranteed compensation in every credit institution or credit union amounted to EUR 15 000 (LVL 10 542) per person. In 2008, the guaranteed compensation would grow until EUR 20 000 (LVL 14 056), which is equal to the minimum guaranteed compensation determined in the EU.

According to information collected by the Commission, of total depositor accounts opened with the Latvian banking system in 2007, balance of over 97% accounts did not exceed EUR 15 000 (LVL 10 542), thus in the reporting year the full compensation was guaranteed to 97% of depositors in Latvia.

The Commission conducts the collection and management of the Deposit Guarantee Fund (DGF) assets. At the end of 2007, DGF accounted for 66.6 million lats. Income from the DGF management, which raises the amount of DGF assets during the reporting year, amounted to 2.4 million lats.

The Consultative Council monitors collection of assets in the DGF and payment of guaranteed compensation. In case of inaccessibility of deposits (pursuant to a court's ruling regarding liquidation of a deposit taker or initiating bankruptcy procedure) the Commission implements the creditor's right of demand to the bank or credit union and performs payment of guaranteed compensation not later than in three months from the date of occurrence of deposit inaccessibility. For exceptional cases the term can be extended up to one year. Since the DGF was established, none of its assets have been used to pay compensation, as there have been no instances of inaccessible deposits in the Latvian banking and credit union system.

Figure 1
GROWTH IN GUARANTEED COMPENSATION PER DEPOSITOR IN THE YEARS 1998–2008
(at the beginning of period; lats)



Fund for the Protection of the Insured

The Fund for the Protection of the Insured (FPI) was created in 1999 in order to protect the interests of insured persons in case of an insurance company's bankruptcy.

The assets of the FPI consist of deductions in the amount of 1% of the gross sum of insurance premiums received from physical persons for the classes of insurance specified by law. At the end of 2007, FPI accounted for 3.7 million lats. Income from management of FPI assets in the reporting year amounted to 127.3 thousand lats.

Only a policyholder, natural person, may receive insurance indemnity in case of insurer default:
1) for life insurance policies – 100% of the insurance indemnity, but no more than 2 000 lats per insured person;
2) for other classes of insurance as established by law – 50% of the insurance indemnity, but no more than 2 000 lats per insured person.

The Commission organizes the collection of assets in the FPI and the payment of guaranteed insurance indemnity. Whereas the Consultative Council monitors collection of assets in the FPI and the payment of guaranteed insurance indemnity. The guaranteed insurance indemnity is paid only after initiating bankruptcy procedure at the insurance company. The Commission implements the creditor's right of demand to insurer.

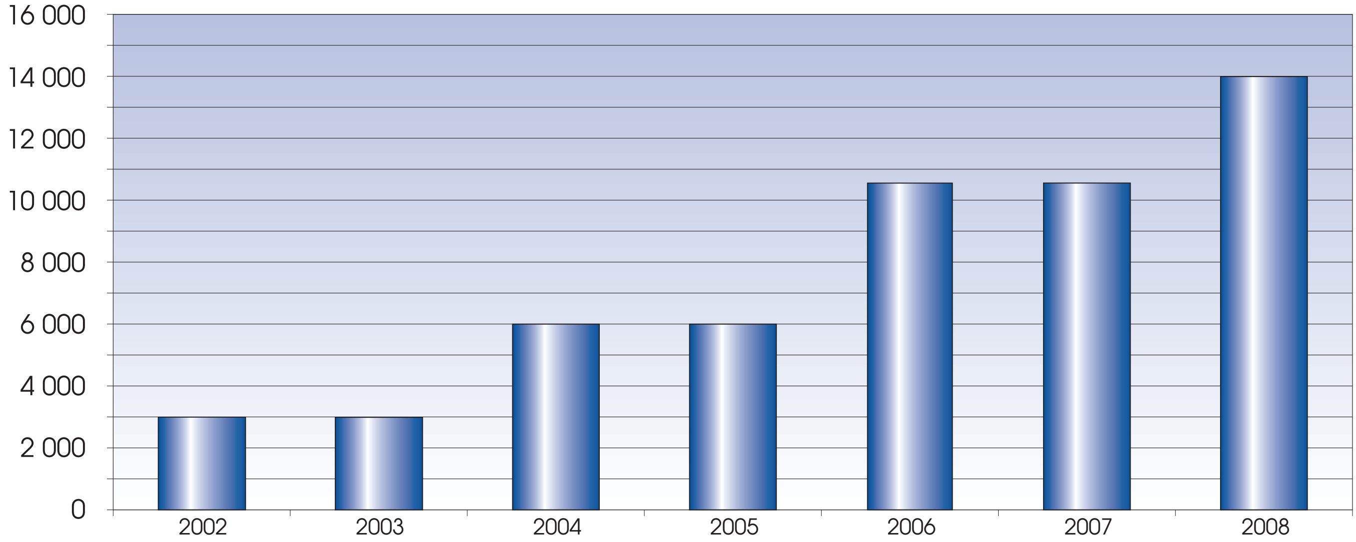
Since the commencing of activities of the FPI, to protect the interests of insured persons in the case of an insurance company's bankruptcy 8 671 lats of the FPI assets have been paid in guaranteed insurance indemnities.

Protection of financial instruments market clients (investors)

As from 1 January 2002, the Investor Protection Law has been in force in Latvia providing a system of protection for investors. In cases when the providers of investment services (banks, investment management companies and investment firms) are incapable of fulfilling their contractual obligations, investors have the right to receive compensation. Failure to meet obligations is compensated at 90% of the irrevocably lost value of financial instruments, or of losses incurred by the non-performance of investment services.

In 2007, compensation at 90% of the irrevocably lost value of financial instruments, or of losses incurred by the non-performance of investment services was guaranteed for an investor, but not more than EUR15 000 (LVL 10 542). In 2008, the guaranteed compensation would be EUR 20 000 (LVL 14 056) (see Fig. 2).

Figure 2
GROWTH IN GUARANTEED COMPENSATION PER INVESTOR IN YEARS 2002–2008
(at the beginning of period; lats)



Contrary to accumulation of funds, the investor protection mechanism developed by DGF and FPI prescribes that funding meant for compensation has not been accumulated in the fund, but in cases when an investment service provider fails to fulfil obligations, the Commission, on the basis of quarterly reports on financial instruments portfolio submitted by other market participants, calculates proportion of payment by every market participant, investment service provider, in the account opened with the Bank of Latvia for guaranteeing compensations.
If necessary, the Commission organizes and monitors payments of market participants for compensations, examines validity of compensation claims and ensures payment of compensation. By the end of the reporting period, the Commission had received no such applications.

Development of normative enactments

To ensure conformity of the normative acts, regulating Latvia's financial and capital market, with the provisions of the EU directives and better international supervisory practice, in total 14 amendments to 12 laws were drafted and took effect in 2007 along with six regulations issued by the Commission and nine regulatory amendments.

Draft laws

Amendments to the **Law on the Financial Instruments Market** were drawn up to transpose into Latvian legislation requirements of the Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC. The Law prescribes uniform requirements for all issuers whose securities are admitted to trading on a regulated market, irrespective of whether they are listed on an official or any other list.

In 2007, amendments to the **Law on the Financial Instruments Market** were worked out to implement provisions arising from Directive 2004/39/EC of the European Parliament and of the Council on markets in financial instruments (MiFID), aiming at further promotion of integration of the EU financial instruments market by setting unified requirements for provision of investment services and at the same time protecting interests of investors. Amendments stipulated in detail managerial requirements and professional criteria for market participants regarding elimination of conflict of interest, execution of customer orders, provision of best possible service as well as information on service for customers. New investment service – maintenance of multilateral trading system - was envisaged in the amendments. The multilateral trading system would be operated by an organizer of a regulated market authorized to organize the regulated market, an investment firm authorized to provide services as well as credit institution authorized to provide investment services.

At the close of 2007 amendments to the **Law on Investment Management Companies** were drafted to implement the requirements of European Commission Directive 2007/16/EC of 19 March 2007 implementing Council Directive 85/611/EEC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) as regards the clarification of certain definitions into the Latvian legislation.

To introduce the principle of one stop agency to facilitate submission of annual reports and accounts of banks, financial institutions and insurance companies to public authorities amendments to the following laws were formulated: **Credit Institution Law, Credit Union Law, Law on Insurance Companies and Supervision Thereof, Law on Investment Management Companies, Law on the Financial Instruments Market** as well as **Law on Private Pension Funds**. The above amendments provided that as of 1 July 2008, an annual report would be submitted only to the State Revenue Service which would forward it in an electronic format to the Registry of Enterprises and the Registry of Enterprises in turn would publish a notification in the newspaper Latvijas Vēstnesis (Official Gazette) that information of annual report has been entered into the registration file of relevant authority. The annual report should be placed also on the Internet website to ensure free access for the public.

Implementation of Basel Capital Accord II (EU directives 2006/48/EC and 2006/49/EC)

Continuing implementation of Directive 2006/48/EC of the European Parliament and of the Council relating to the taking up and pursuit of the business of credit institutions and Directive 2006/49/EC of the European Parliament and of the Council on the capital adequacy of investment firms and credit institutions (Directives) in Latvia, in 2007 amendments to the **Credit Institution Law** and **Law on Financial Instruments Market** were passed, as well as a number of regulations: **Regulations on the Calculation of Minimum Capital Requirements, Regulations on the Compliance with Restrictions on Exposures, Regulations for Establishing an Internal Control System, Regulations on the Information Disclosure, Regulations on the Recognition of External Credit Assessment Institution and Regulations on Obtaining Permits for Using Internal Ratings Based Approach, Advanced Measurement Approach, Internal Model Approach and Internal Value-at-Risk Model.** To provide methodological support for proper application of regulations and completion of relevant reports, the Commission held a presentation of the new regulations and training for market participants as well as presented the trial calculation of minimum capital requirements and performed data aggregation.

On the basis on the guidelines developed by the Committee of European Banking Supervisors (CEBS) regarding common reporting framework (COREP) for the calculation of minimum capital requirements and own funds in all the EU Member States, **Regulations on the Preparation and Submission of Reports on the Calculation of Minimum Capital Requirements and Own Funds** were drawn up that include 13 reporting templates for the calculation of minimum capital requirements and own funds. Having regard of the guidelines developed by the CEBS regarding consolidated financial reporting framework (FINREP), **Regulations on the Consolidated Supervision** were specified to bring financial report templates for consolidated group supervision in line with FINREP, as well as lower reporting frequency determined.

International Cooperation
European Union institutions

Involvement in the EU institutions is a main direction of the Commission's international cooperation, aimed at observation of Latvia's commitments arising from the accession treaty and falling within the Commission's competence as well as protection of the Latvian financial sector. Participation of the Commission in the EU institutions remained unchanged in the reporting year. The Commission's experts continued actively taking part in work of the EU institutions: in the meetings of the Financial Services Committee (FSC) under Lamfalussy framework, Level 1, as well as in the committees set up by the European Central Bank (ECB) and their working groups in the area of financial services.

In 2007, the European Council started revising proposals submitted by the European Commission for the new European Union Directive on the taking-up and pursuit of the Business of Insurance and Reinsurance (draft directive), implementation of which is planned for 2012.

The draft directive consolidates currently effective directives that regulate activities of life insurers, non-life insurers, reinsurance and insurance groups (insurers and reinsurers), and implements the new system for capital adequacy determination and supervision (Solvency II) for insurers and reinsurers. Thus the key changes in draft directive cover the calculation of required solvency margin and available solvency margin, calculation of technical provisions and supervision of insurance groups. The Commission's specialists actively participated in discussions on the draft directive held by the Council's working group, formulated national positions and instructions for the draft directive generally or in detail.

The Commission's experts, representing the Ministry of Finance, participated in the following committees and their working groups: the European Banking Committee (EBC) Level 2, European Insurance and Occupational Pensions Committee (EIOPC)), European Securities Committee (ESC). The Commission actively participated in the committees of Lamfalussy Level 3: Committee of European Securities Regulators (CESR), Committee of European Banking Supervisors (CEBS) and Committee of European Insurance and Occupational Pension Supervisors (CEIOPS). All the Level 3 committees make every effort to ensure convergence of supervision practice in the EU, as well as review issues specific to the respective sector. The Committee of European Banking Supervisors has been strongly committed to ensuring the implementation of Basel Capital Accord II, as well as formulates its opinion regarding revision of instruments to be included in equity, large exposure limits and liquidity risk management for submission to the European Commission. Attention of the Committee of European Securities Regulators was devoted to the implementation of the Markets in Financial Instruments Directive (MiFID). Development of technical recommendations for the practical application of basic guidelines within the Solvency II framework and quantitative impact assessment of Solvency II were in the limelight of the Committee of European Insurance and Occupational Pension Supervisors.

In the second half of 2007 following a financial turmoil on the international financial markets priorities were adjusted and additional issues included on the agenda of the Lamfalussy framework Levels 2 and 3 committees. The key priorities in the European Council's ECOFIN roadmap of October 2007 were as follows:
1) enhancement of disclosure of information;
2) improvement of prudential supervision and risk management instruments;
3) financial instruments valuation standards;
4) market functioning (external credit assessment institutions).
These are still high priorities in the year 2008.

In the reporting year, the Commission's experts drafted the Latvian national position and instructions for the European Council's ECOFIN, the Permanent Representatives Committee (COREPER) and the Economic and Financial Committee (EFC) meetings, to present their stance and proposals for the EU draft legal enactments regarding the financial and capital market oversight. Overall, the Commission developed 16 national position drafts and instructions for draft directive within Solvency II and its impact on the activities of insurers and reinsurers in Latvia, introduction of the European Code of Conduct for Clearing and Settlement and integration of clearing and settlement system, as well as enhancement of the European single market for investment funds. Required changes in regulatory norms of the draft Payment Service Directive and draft Directive regarding the criteria and timescale of the assessment procedure applicable by supervisory authorities in cases where qualifying holdings are acquired and increased in the financial sector were also evaluated.

The Commission within its competence reviewed and expressed its opinion also on 60 draft positions and instructions prepared by other institutions. All efforts were made to implement the EU Lisbon strategy, as well as enhancement of draft directive aiming to harmonise consumer credit contracts and draft directive regarding portability of supplementary pension rights and finalizing the draft regulation on the law applicable to contractual obligations.

Cooperation with foreign financial supervisory institutions

In the reporting year, the Commission efficiently cooperated also with foreign supervisory authorities and taking account of cross-border activities by market participants expanded cooperation with partners and entered into one new agreement – the Memorandum of Understanding between the New York State Banking Department and the Commission concerning their cooperation and exchange of information in the field of supervision of banks and their cross-border establishments.

In total, the Commission has signed 24 bilateral cooperation agreements up to now of which 13 agreements are concluded with foreign credit institution supervisory authorities. The Commission has entered into Memorandum of Understanding with the Finnish Financial Supervision Authority regarding cooperation in the supervision of Nordea Bank Finland Plc. Two agreements on sharing information without signing a cooperation agreement in writing have been already reached: the Office of the Comptroller of the Currency (the U.S. federal banking supervision agency under the United States Department of the State Treasury) and the Swiss Federal Banking Commission. Moreover, the Commission has signed also three multilateral cooperation: Memorandum of Understanding on Co-operation between the Banking Supervisors, Central Banks and Finance Ministries of the European Union in Financial Crisis Situation, Memorandum of Understanding on Co-operation between Payment Systems Overseers and Banking Supervisors in Stage Three of EMU; Memorandum of Understanding on High-Level Principles of Co-operation between Banking Supervisors and Central Banks of the EU in Crisis Management Situations.

Principal Objectives of the Financial and Capital Market Commission for 2008

1. Considering chances and challenges offered to Latvia by its participation in the EU and global financial markets, and for the purpose to become an efficient and dynamic supervisory institution that ensures high standards in the financial service area and enhances the financial and capital market development in Latvia, the Commission has decided to develop a new strategy for the period from 2009 to 2011.

2. Continuing the implementation of the EU directives in the Latvian financial and capital market, in 2008 the Commission is planning:

- to participate in the project managed by the Ministry of Finance regarding the formulation of the law on payment services and regulations on the compliance with rules for activities of payment service providers;

- to make amendments to the Law on the Financial Instruments Market to transpose Directive of the European Parliament and of the Council on the exercise of voting rights by shareholders of companies whose shares are admitted to trading on a regulated market;

- to standardize requirements for the acquisition and increase of a qualifying holding in overall financial sector, to draw up amendments to the Credit Institution Law, Law on Insurance Companies and Supervision Thereof, Law on the Financial Instruments Market, Law on Investment Management Companies and Reinsurance Law;

- to develop regulations on the criteria for the compliance of investment fund investment objects with the provisions of the Law on Investment Management Companies;

- to revise the Regulations for Assessing Assets and Off-balance-sheet Liabilities in order to be in line with the International Accounting Standards (IAS), International Financial Reporting Standards (IFRS) and recommendations of the Basel Committee on Banking Supervision (BCBS);

- in order to supplement the regulations with an annex according to which classification of specialized credit exposures is determined depending on risk degree, to draft amendments to the Regulations on the Calculation of Minimum Capital Requirements, as well as to draft the procedure for issuing permits in order to ensure the compliance of the procedure for issuing permits with the requirements for quality management system;

- to develop and approve the regulations for insurers regarding implementation of stress testing and preparation of report of stress testing results in order to improve the assessment process for insurers' operational risk and possible losses.

3. To provide an interactive financial and statistical report submission system and publishing of templates, the Commission has decided to implement an electronic data reporting system. The system would ease the existing process for submission of statistical reports, which was based on the e-mail system, as well as ensure accessibility to up-to-date reporting templates.

The full text of the Commission's operation plan in Latvian is available on the Commission's website at www.fktk.lv (Section *Komisija/Par mums/Darba plāni*).

FINANCIAL STATEMENTS OF THE FINANCIAL AND CAPITAL MARKET COMMISSION FOR 2007

Management Report

The Financial and Capital Market Commission (hereinafter referred to also as the Commission) commenced its activities on 1 July 2001 and has been operating in accordance with the Law on the Financial and Capital Market Commission.

On 15 December 2006, based on Article 17 (9) of the Law on the Financial and Capital Market Commission, by Decision No. 208, the Commission's Board approved the Budget of the Financial and Capital Market Commission for 2007, thereby specifying the financing for activities of the Commission and the use of these funds. Decision No. 147 of 26 October 2007 of the Commission's Board On the Approval of Amendments to the Budget of the Financial and Capital Market Commission for 2007 specified additional financing and actual expenses in the Commission's budget for 2007. The financial and capital market participants made payments for financing the activities of the Commission pursuant to the Regulations on the Amount of Payments by Financial and Capital Market Participants for Financing the Financial and Capital Market Commission and on the Procedures for Submission of Reports for the Year 2007, approved by the Commission's Board on 15 December 2006.

The Commission conducted accounting in accordance with the Law on Accounting and, as an autonomous public institution possessing state property, complied with the basic principles of accounting for budgetary institutions set out in the regulations issued by the Cabinet of Ministers.

During the reporting year, pursuant to Article 6 of the Law on the Financial and Capital Market Commission, the Commission managed the Deposit Guarantee Fund and the Fund for the Protection of the Insured (hereinafter referred to also as the Funds). For the purposes of a clearer perception, assets of the Funds managed by the Commission are disclosed separately in the balance sheet.

In 2007, assets of the Funds were invested in accordance with the investment policies and investment procedures specified for the Deposit Guarantee Fund and the Fund for the Protection of the Insured, approved by the Commission's Board on 15 September 2006, which stipulate asset investments only in the primary market of securities, and in the currency, in which payments from the Deposit Guarantee Fund and the Fund for the Protection of the Insured are to be made. The said investment policies provide for keeping of at least 10% of each Fund's assets liquid: either in an account held with the Bank of Latvia or invested in debt securities whose term of redemption does not exceed one year. In 2007, assets of the Funds managed by the Commission were invested in compliance with the requirements of the Agreement on Investing Assets of the Deposit Guarantee Fund and the Fund for the Protection of the Insured in Latvian State Treasury Securities, entered into between the Commission and the State Treasury.

As the Commission falls within the definition of a contracting authority provided by the Law on Public Procurement, all procurements for ensuring the Commission's activities were made in compliance with the requirements of the said law.

On 13 November 2007, an agreement on the audit of the Commission's financial statements for 2007 was entered into with Ernst & Young Baltic SIA, which was represented by Sworn Auditor of the Republic of Latvia Iveta Vimba (certificate No. 153).

The State Audit Office did not perform any audits relating to activities of the Commission in the reporting year.

Funds of the Commission

At the end of 2007, assets of the Commission totalled 72 620 thousand lats, of which 70 268 thousand lats were managed trust assets, i.e. assets of the Deposit Guarantee Fund and the Fund for the Protection of the Insured. In 2007, activities of the Commission were financed solely from payments made by financial and capital market participants. At the end of 2007, the Commission's equity or net assets accounted for 2 136 thousand lats, which had increased by 281 thousand lats as compared to 2006.

Ensuring Activities of the Commission

In 2007, the revenues of the Commission were 3 405.7 thousand lats, or 0.51% more than the planned revenues, as laid down in the Commission's budget for 2007 (3 388 thousand lats). When approving the budget for the year 2007, the Board of the Commission specified that if the Commission's revenues from payments of any sector of financial and capital market participants for 2007 exceed the planned revenues for the relevant sector, the Commission calculates the share of this excess payment according to the proportion of payments in the relevant sector by every financial and capital market participant in 2007 and records as prepayment for financing the Commission in 2008. The Commission's excess of revenues over the planned revenues in 2007 was mainly made of interest income earned from the cash balance in the Commission's current account. Total expenses of the Commission in 2007 were 3 124 thousand lats. According to the Commission's budget planning, the Commission's expenses, excluding provisions for vacation, in 2007 accounted for 3 183 thousand lats, which was by 5.4% less than the planned expenses (3 365 thousand lats). The excess of revenues over expenses in 2007 was 281.4 thousand lats. The Commission's annual budget result has been positive since 2004, whereas in 2002 and 2003, the actual revenues of the Commission were lower than the actual expenses, due to the fact that the funds allocated for the establishment of the Commission and commencement of its activities in 2001 were invested in long-term assets, whose amortisation effect increased the Commission's expenses, while having no impact on the cash flow.

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

In the reporting period, revenues of the Deposit Guarantee Fund from credit institution and credit union payments constituted 15 560 thousand lats, while revenues of the Fund for the Protection of the Insured, received from insurers, constituted 1 053.4 thousand lats. Revenues from investments made by the Deposit Guarantee Fund were 2 439 thousand lats, while by the Fund for the Protection of the Insured, 127.3 thousand lats. Total assets of these Funds increased by 19 182 thousand lats, or 37.5%, that is, assets of the Deposit Guarantee Fund rose by 18 001 thousand lats, or 37%, while assets of the Fund for the Protection of the Insured, by 1 181 thousand lats, or 47%. At the end of 2007, net financial assets of the Deposit Guarantee Fund comprised 66 575.4 thousand lats while net financial assets of the Fund for the Protection of the Insured, 3 692.5 thousand lats.

In the reporting period, the Commission invested assets of the Funds in both short-term and long-term Latvian State Treasury securities. Of the total securities portfolio of the Funds at the end of 2007, 58% were placed in long-term while the rest in short-term securities. Of the securities portfolio of the Deposit Guarantee Fund, 58% were invested in long-term securities while the rest in short-term securities. As regards the securities portfolio of the Fund for the Protection of the Insured, the corresponding figures were 52% for long-term securities and 48% for short-term securities. In 2007, the profitability of assets of the Deposit Guarantee Fund reached 4.42%, while that of the Fund for the Protection of the Insured, 4.36%. The profitability was calculated by dividing the sum of investment revenues of the relevant Fund during 2007 by the average asset value of the Fund during 2007.

Chairman of the Financial and
Capital Market Commission

Uldis Cērps

25 April 2008

Balance Sheet
ASSETS

	Note	31.12.2007	31.12.2006
			(lats)
ASSETS OF THE FUNDS			
LONG-TERM INVESTMENS		**37 305 418**	**32 275 424**
Investments by the Funds in securities	3	37 305 418	32 275 424
CURRENT ASSETS		**32 962 478**	**18 810 336**
Receivables		**4 538 013**	**3 667 016**
Due from market participants to the Funds	5	4 537 949	3 666 952
Settlements with the administrators related to guaranteed compensation payments	13	64	64
Investments by the Funds in securities	3	**26 653 866**	**15 142 466**
Cash	2	**1 770 599**	**854**
TOTAL ASSETS OF THE FUNDS		**70 267 896**	**51 085 760**
ASSETS OF THE COMMISSION			
LONG-TERM INVESTMENS	4	**97 169**	**68 108**
Intangible assets		47 853	29 038
Fixed assets		41 095	36 853
Prepayments for long-term investments		8 221	2 217
CURRENT ASSETS		**2 255 253**	**1 973 174**
Inventories		**80**	**101**
Accounts receivable		**229 231**	**346 169**
Due from market participants to the Commission	6	225 317	343 048
Other receivables	12	3 013	2 199
Due from the staff		901	922
Prepaid expenses	9	**6 906**	**10 554**
Cash		**2 019 036**	**1 616 350**
TOTAL ASSETS OF THE COMMISSION		**2 352 422**	**2 041 282**
TOTAL ASSETS		**72 620 318**	**53 127 042**

The accompanying notes on pages 25 to 32 form an integral part of these financial statements.

Balance Sheet

LIABILITIES

	Note	31.12.2007	31.12.2006
			(lats)
LIABILITIES OF THE FUNDS			
EQUITY	10	**70 267 896**	**51 085 760**
Net financial assets of the Funds (budget result)		70 267 896	51 085 760
TOTAL LIABILITIES OF THE FUNDS		**70 267 896**	**51 085 760**
LIABILITIES OF THE COMMISSION			
EQUITY	10	**2 136 448**	**1 855 090**
Net assets of the Commission		2 136 448	1 855 090
PAYABLES		**215 974**	**186 192**
Prepayments to the Commission by market participants	7	88 523	5 011
Accounts payable to suppliers	11	24 927	18 826
Overpaid taxes	8	428	1 168
Provision for vacation		102 096	161 187
TOTAL LIABILITIES OF THE COMMISSION		**2 352 422**	**2 041 282**
TOTAL LIABILITIES		**72 620 318**	**53 127 042**

The accompanying notes on pages 25 to 32 form an integral part of these financial statements.

Chairman of the Financial and
Capital Market Commission — Uldis Cērps

Head of
the Resource Management Division — Rita Vanaga

25 April 2008

Revenue and Expense Statement

(lats)

	Note	2007	2006
REVENUES			
REVENUES RELATED TO SUPERVISION			
OF CREDIT INSTITUTIONS AND CREDIT UNIONS		2 333 147	1 974 243
Payments by the Bank of Latvia		-	240 000
Payments by credit institutions		2 324 280	1 725 658
Payments by credit unions		8 867	8 585
REVENUES RELATED TO INSURANCE SUPERVISION		874 070	756 269
Payments by life assurance companies		75 410	70 161
Payments by other insurance companies		798 660	686 108
REVENUES RELATED TO SUPERVISION			
OF THE SECURITIES MARKET AND PENSION FUNDS		155 008	143 724
Payments by securities market participants		115 358	110 994
Payments by private pension funds		39 650	32 730
OVERDUE PAYMENTS		202	36
INCOME FROM INTEREST ON THE BALANCE			
OF THE COMMISSION'S CURRENT ACCOUNT		43 259	32 101
TOTAL REVENUES		**3 405 686**	**2 906 373**
EXPENSES			
Staff remuneration and other payments		(2 297 088)	(2 045 032)
Staff remuneration and other payments	14	(1 903 069)	(1 691 043)
State social insurance compulsory contributions		(394 019)	(353 989)
Provision for vacation		59 091	(37 258)
Staff insurance	15	(124 247)	(106 168)
Improvements of professional skills and business trips	16	(193 757)	(158 870)
Telecommunication and information		(39 223)	(37 166)
Public information and external and internal communications		(25 166)	(20 120)
Maintenance expenses	17	(308 365)	(260 946)
Professional services	18	(82 065)	(20 123)
Participation in international organisations and			
co-financing for attache operation in Brussels	(78 286)	(54 321)	
Depreciation/amortisation/write-off of capital investments	4	(35 222)	(64 636)
TOTAL EXPENSES		**(3 124 328)**	**(2 804 640)**
EXCESS OF REVENUES OVER EXPENSES BUDGET RESULT		**281 358**	**101 733**

The accompanying notes on pages 25 to 32 form an integral part of these financial statements.

Chairman of the Financial and Capital Market Commission — Uldis Cērps

Head of the Resource Management Division — Rita Vanaga

25 April 2008

Cash Flow Statement

	Note	2007	(lats) 2006
RECEIPTS			
RECEIPTS RELATED TO SUPERVISION OF CREDIT INSTITUTIONS AND CREDIT UNIONS		2 373 663	2 012 527
Payments by the Bank of Latvia		-	240 000
Payments by credit institutions		2 364 853	1 764 026
Payments by credit unions		8 810	8 501
RECEIPTS RELATED TO SUPERVISION OF INSURANCE		999 613	958 488
Payments by life assurance companies		130 574	99 890
Payments by other insurance companies		869 039	858 598
RECEIPTS RELATED TO SUPERVISION OF THE SECURITIES MARKET AND PENSION FUNDS		190 194	165 245
Payments by securities market		155 618	115 628
Payments by private pension funds		34 576	49 617
OVERDUE PAYMENTS		202	36
INCOME FROM INTEREST ON THE BALANCE OF THE COMMISSION'S CURRENT ACCOUNT		43 259	32 101
TOTAL RECEIPTS		**3 606 931**	**3 168 397**
PAYMENTS			
Staff remuneration and other payments		(2 293 229)	(2 043 336)
Staff remuneration and other payments		(1 898 684)	(1 689 825)
State social insurance compulsory contributions		(394 545)	(353 511)
Staff insurance		(124 183)	(106 173)
Improvements of professional skills and business trips		(196 455)	(158 350)
Telecommunication and information		(38 410)	(37 786)
Public awareness campaigns and external and internal communications expenses		(24 755)	(22 256)
Maintenance expenses		(308 414)	(259 687)
Professional services		(83 127)	(18 432)
Participation in international organisations and co-financing for attache operation in Brussels		(77 340)	(44 533)
TOTAL PAYMENTS		**(3 145 913)**	**(2 690 553)**
INVESTMENT ACTIVITIES			
Capital expenditure		(58 332)	(30 044)
TOTAL INVESTMENT ACTIVITIES		**(58 332)**	**(30 044)**
Net change in cash during the reporting period		**402 686**	**447 800**
Cash balance at the beginning of the reporting period		**1 616 350**	**1 168 550**
Cash balance at the end of the reporting period		**2 019 036**	**1 616 350**

The accompanying notes on pages 25 to 32 form an integral part of these financial statements.

Chairman of the Financial and
Capital Market Commission — Uldis Cērps

Head of
the Resource Management Division — Rita Vanaga

25 April 2008

Statement of Changes in Equity

(lats)

	Note	Equity (net assets) of the Commission	Net financial assets of the Deposit Guarantee Fund	Net financial assets of the Fund for the Protection of the Insured	Equity (net financial assets) of the Funds
					2
Budget result 31.12.2005		**1 756 236**	**34 490 740**	**1 854 758**	**36 345 498**
Fixed asset depreciation/ write-off in 2006 charged to the budget result	1	**(2 879)**	-	-	-
Budget result of the reporting period		**101 733**	14 083 285	656 977	**14 740 262**
Budget result 31.12.2006		**1 855 090**	**48 574 025**	**2 511 735**	**51 085 760**
Budget result of the reporting period		**281 358**	18 001 389	1 180 747	**19 182 136**
Budget result 31.12.2007		**2 136 448**	**66 575 414**	**3 692 482**	**70 267 896**

The accompanying notes on pages 25 to 32 form an integral part of these financial statements.

Chairman of the Financial and Capital Market Commission — Uldis Cērps

Head of the Resource Management Division — Rita Vanaga

25 April 2008

Notes to the Financial Statements

The Financial and Capital Market Commission was established and operates under the Law on the Financial and Capital Market Commission.

The objective of the Commission is 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.

1. Accounting Policies of the Commission

Basis for Preparation of the Financial Statements
The financial statements were prepared by using as guidelines the Regulation No. 749, On the Procedure for Preparation of Annual Reports for State and Local Government Budgetary Institutions, issued by the Cabinet on 13 November 2007.

The Commission's accounting has been conducted in compliance with the Cabinet of Ministers of the Republic of Latvia Regulations No. 867 of 15 November 2005 On Accounting Procedures for Budgetary Institutions.

The accounting principles applied for the reporting period and previous years were used consistently.

The Commission presented all assets and liabilities, including those of the Deposit Guarantee Fund and the Fund for the Protection of the Insured, in a single balance sheet. The Commission reflected all revenues and expenses related to its financing as well as revenues and expenses of the Deposit Guarantee Fund and the Fund for the Protection of the Insured as separate statements of income and expenses. The cash flow statement and the statement of income and expenses of the Deposit Guarantee Fund and the Fund for the Protection of the Insured were prepared as notes to the financial statements.

The long-term assets acquired from the budget for the Commission's establishment and commencement of activities at the launch of the Commission's activities were used to ensure activities of the Commission; consequently, these assets were included in the general balance sheet of the Commission, as well as asset depreciation/amortisation or write-off was included in the Commission's statement of income and expenses.

Principles Applied in Preparing the Financial Statements
- The financial statements, except for the cash flow statement, are prepared in compliance with the principle of accrual-based accounting. It provides for recognition of transactions and events in the financial statements at the date of their occurrence, irrespective of the related cash flows. Revenues are derived on the basis of business operations performed by financial and capital market participants, which are reported and from which payments are to be calculated. Expenses are recognised at the date of their occurrence, including accrued vacation expenses proportionate to the time actually worked. Accrued vacation expenses shall be specified for each staff member for his or her paid vacation days accrued up to 31 December of the respective calendar year.
- Assets are recognised at historic cost. Assets are booked on the date of their acquisition in the amount of paid cash or cash equivalents, or at the fair value of other consideration provided plus any other costs related directly to acquisition of assets.
- Transactions and other events are reflected by taking into account the principle of substance over form, stating that transactions and events shall be recognised and disclosed according to their contents and economic substance and not only according to their legal form.
- The financial statements have been prepared on an on-going concern basis.

Long-term Investments
Long-term investments were recognised by taking as guidelines the basic principles set out in the Cabinet of Minister of the Republic of Latvia Regulations No. 867 of 15 November 2005, On Accounting Procedures for Budgetary Institutions. Depreciation rates for long-term investments, acquired beginning from 2006, were applied in compliance with the Regulation No. 440, On Fixed Asset Depreciation Rates for Budgetary Institutions and Application Conditions, issued by the Cabinet of Ministers of the Republic of Latvia on 21 June 2005, which stipulates the following annual depreciation rates:

- computers and equipment 20%;
- other fixed assets 10%.

Whereas depreciation rates for long-term investments, acquired before 2006, were applied in compliance with Regulation No. 96, On Fixed Asset Depreciation Rates for Budgetary Institutions, issued by the Cabinet of the Republic of Latvia on 6 March 2001, which stipulated the following annual depreciation rates:

- computers and equipment 35%;
- other fixed assets 20%.

The depreciation for the Commission's fixed assets is calculated until their residual value reaches 5 lats as provided for by the Regulations No. 96 of the Cabinet of Ministers of 6 March 2001 On Fixed Asset Depreciation Rates for Budgetary Institutions. For reconstructing long-term investments acquired before 2006, their depreciation rates have been changed in compliance with provisions on fixed asset depreciation rates of the Regulation No. 440, On Fixed Asset Depreciation Rates for Budgetary Institutions and Application Conditions, issued by the Cabinet of Ministers of the Republic of Latvia on 21 June 2005

The amount of depreciation calculated for fixed assets was included into the Commission's statement of income and expenses, except for the fixed assets taken over from budgetary institutions (the Insurance Supervision Inspectorate, the Securities Market Commission and the Deposit Guarantee Fund Administration) on 1 July 2001, the depreciation of which was directly charged against the book value of fixed assets in the Commission's balance sheet still in 2006 and the Commission's equity (net assets). Such a method is provided by the Regulations No. 96 of the Cabinet of Ministers of 6 March 2001 On Fixed Asset Depreciation Rates for Budgetary Institutions, for in the respective budgetary institutions fixed assets were expensed in their full value at the date of acquisition and a corresponding fixed asset fund for this amount was credited to equity. In 2007, no depreciation for these fixed assets was developed.

Securities

Securities in the possession of the Commission are being held to maturity. The valuation of long-term securities is performed using the effective interest rate amortisation method. The valuation of short-term securities is performed using the straight-line discount amortisation method.

Accounts Receivable

The Commission steadily follows that settlements are made in due time. In case of a doubtful debtor, the debtor will be excluded from the balance sheet item *Accounts receivable* by decreasing revenues of the Commission in that reporting period in which the debtor has been excluded.

2. Actual Result of Revenues and Expenses and Cash Flows of the Deposit Guarantee Fund and the Fund for the Protection of the Insured (in lats)

	Result of revenues and expenses in 2007	Result of revenues and expenses in 2006
REVENUES		
Payments to the Deposit Guarantee Fund	15 560 100	12 652 612
Payments by credit institutions	15 549 850	12 643 362
Payments by credit unions	10 250	9 250
Payments to the Fund for the Protection of the Insured	1 053 414	578 417
Payments by life assurance companies	420 922	144 444
Payments by other insurance companies	632 492	433 973
Income from investments	2 566 745	1 509 066
Income of the Deposit Guarantee Fund	2 439 443	1 430 506
Income of the Fund for the Protection of the Insured	127 302	78 560
OVERDUE PAYMENTS	1 877	167
TOTAL REVENUES	**19 182 136**	**14 740 262**
EXPENSES		
Guaranteed compensation payments	-	-
TOTAL EXPENSES	-	-
RESULT	**19 182 136**	**14 740 262**

	Cash flow in 2007	Cash flow in 2006
FINANCING		
Payments to the Deposit Guarantee Fund	14 872 434	11 933 964
Payments by credit institutions	14 862 565	11 924 857
Payments by credit unions	9 869	9 107
Payments to the Fund for the Protection of the Insured	870 083	516 405
Payments by life assurance companies	319 719	123 936
Payments by other insurance companies	550 364	392 469
OVERDUE PAYMENTS	1 877	167
CASH FLOW FROM FINANCING	**15 744 394**	**12 450 536**
INVESTMENT ACTIVITIES		
INVESTMENT ACTIVITIES		
(Increase in) investments	(16 028 087)	(14 180 350)
(Increase in) debt securities in the Deposit Guarantee Fund	(15 302 985)	(13 584 540)
(Increase in) debt securities in the Fund for the Protection of the Insured	(725 102)	(595 810)
Income from investments	2 053 438	1 730 455
Interest payments to the Deposit Guarantee Fund	1 949 339	1 650 967
Interest payments to the Fund for the Protection of the Insured	104 099	79 488
CASH FLOW FROM INVESTMENT ACTIVITIES	**(13 974 649)**	**(12 449 895)**
EXPENSES		
Compensation payments from the Fund for the Protection of the Insured	-	-
TOTAL EXPENSES	-	-
CASH FLOW RESULT	**1 769 745**	**641**
Cash balance at the beginning of the reporting period	**854**	**213**
Cash balance at the end of the reporting period	**1 770 599**	**854**

3. Investments in Securities

This item contains the purchased Latvian State Treasury securities. The value of long-term securities was disclosed in the balance sheet at amortised cost. The value of short-term securities was disclosed in the balance sheet at the value calculated by using discount amortisation method.

Securities of the Funds (in lats) were placed in the following Latvian Government securities issues:

Issue No.	Issue date	Maturity date	Annual rate of return (%)	Nominal value	**Book value 31.12. 2007**
LV0000580033	02.12.2005	02.12.2015	4.10	20 616 600	19 549 126
LV0000580017	14.02.2003	14.02.2013	4.85	3 785 000	3 980 855
LV0000570059	03.11.2006	03.11.2011	4.98	5 626 300	5 655 473
LV0000570042	06.10.2005	06.10.2010	3.31	6 184 400	6 268 224
LV0000550085	30.03.2007	30.03.2009	5.62	1 772 600	1 851 740
			Long-term investments by funds	37 984 900	**37 305 418**

Issue No.	Issue date	Maturity date	Annual rate of return (%)	Nominal value	**Book value 31.12.2007**
LV0000540912	11.01.2007	11.01.2008	4.34	5 861 700	5 851 925
LV0000540920	06.06.2007	06.06.2008	5.50	7 869 200	7 689 253
LV0000540938	08.08.2007	08.08.2008	5.85	13 578 600	13 112 688
			Short-term investments by funds	27 309 500	**26 653 866**

Issue No.	Issue date	Maturity date	Annual rate of return (%)	Nominal value	**Book value 31.12.2006**
LV0000580033	02.12.2005	02.12.2015	4.10	20 616 600	19 432 935
LV0000580017	14.02.2003	14.02.2013	4.85	3 785 000	3 985 448
LV0000570059	03.11.2006	03.11.2011	5.04	2 572 300	2 588 581
LV0000570042	06.10.2005	06.10.2010	3.31	6 184 400	6 268 460
			Long-term investments by funds	33 158 300	**32 275 424**

Issue No.	Issue date	Maturity date	Annual rate of return (%)	Nominal value	**Book value 31.12. 2006**
LV0000570034	08.05.2002	08.05.2007	5.49	1 618 300	1 633 907
LV0000540904	06.10.2006	06.10.2007	4.83	3 902 100	3 763 272
LV0000540896	02.06.2006	02.06.2007	4.00	7 426 000	7 305 085
LV0000532158	20.10.2006	20.04.2007	4.84	1 592 600	1 569 619
LV0000532141	07.07.2006	05.01.2007	3.75	871 200	870 583
			Short-term investments by funds	15 410 200	**15 142 466**

Allocation of the securities book value for Funds was as follows:

	31.12.2007	**31.12.2006**
Securities of the Deposit Guarantee Fund	60 887 352	45 094 264
Securities of the Fund for the Protection of the Insured	3 071 932	2 323 626
	63 959 284	47 417 890

At the end of the reporting period, the accrued income included in the book value of securities was as follows:

	31.12.2007	**31.12.2006**
Accrued income of the Deposit Guarantee Fund	839 701	545 208
Accrued income of the Fund for the Protection of the Insured	58 273	38 692
	897 974	583 900

4. Long-term Investments

	Book value 31.12.2006	Additions in the reporting period	Write-offs and disposals	Depreciation: Charge in the reporting period	Depreciation: Reversal due to disposals (since acquisition)	Book value 31.12.2007
Intangible assets						
Licences, software and other intangible assets	**29 038**	35 890	(5 092)	(17 035)	5 052	**47 853**
Fixed assets						
Computers and office equipment	**23 175**	21 506	(21 031)	(15 463)	20 791	**28 978**
Other fixed assets	**13 678**	883	-	(2 444)	-	**12 117**
Prepayments for long-term investments	**2 217**	7 985	(1 981)	-	-	**8 221**
	68 108	**66 264**	**(28 104)**	**(34 942)**	**25 843**	**97 169**

Changes in long-term investments in 2007, showing expenses disclosed in the statement of income and expenses:

	Charge	Write-offs or disposals, excluding the accrued depreciation	Total
Depreciation/amortisation/write-off of capital investments charged to the statement of income and expenses	34 942	280	35 222

5. Due from Market Participants to the Funds

This item contains amounts due from financial and capital market participants to the Deposit Guarantee Fund and the Fund for the Protection of the Insured for the fourth quarter ended 31 December 2007 and the fourth quarter ended 31 December 2006, respectively.

	31.12.2007	31.12.2006
Due from market participants to the Deposit Guarantee Fund	4 166 773	3 479 107
Due from credit institutions	4 164 004	3 476 770
Due from credit unions	2 769	2 337
Due from market participants to the Fund for the Protection of the Insured	371 176	187 845
Due from life assurance companies	160 606	59 403
Due from other insurance companies	210 570	128 442
	4 537 949	**3 666 952**

6. Due from Market Participants to the Commission

This item contains amounts due from financial and capital market participants to the Commission on the date set out in the statement.

Due from different segments of financial and capital market participants to the Commission:

	31.12.2007	31.12.2006
Due from credit institutions	212 684	253 256
Due from credit unions	2 206	2 149
Due from life assurance companies	-	66
Due from other insurance companies	-	44 766
Due from investment management companies	10 204	26 827
Due from investment brokerage firms	160	6 587
Due from the Latvian Central Depository and the Riga Stock Exchange	-	9 397
Due from private pension funds	63	-
	225 317	**343 048**

7. Prepayments of Market Participants to the Commission

This item contains amounts prepayments made by the financial and capital market participants for financing the Commission on the date set out in the statement.

Prepayments by different segments of financial and capital market participants to the Commission:

	31.12.2007	31.12.2006
Due from life assurance companies	61 940	-
Due from other insurance companies	25 603	-
Due from the Latvian Central Depository and the Riga Stock Exchange	980	-
Due from private pension funds	-	5 011
	88 523	**5 011**

8. Taxes

Nodokļa veids	**Balance on 31.12.2006**	Calculated for the reporting period	Decreased compulsory contribution result	Paid in the reporting period	**Balance on 31.12.2007**
Contributions to compulsory state social insurance (overcharge)	1 172	544 639	(2 486)	(542 875)	450
Personal income tax (overcharge)	(4)	416 629	-	(416 647)	(22)
	1 168	961 268	(2 486)	(959 522)	**428**

According to the data received from the State Revenue Service, compulsory contributions to State social insurance were decreased in 2006 by the amount that exceeded the maximum limit specified by the Cabinet, i.e. 20 700 lats per tax-payer in 2006.

9. Nākamo periodu izdevumi

	31.12.2007	31.12.2006
Data base subscription fees	2 870	2 560
Software subscription fees	2 140	3 290
Professional literature	915	627
Other prepaid expenses	981	4 077
	6 906	**10 554**

10. Equity

This item represents net assets of the Commission (total budget result) and net financial assets of the Funds managed by the Commission (budget result). Changes thereof are disclosed in the Statement of Changes in Equity and notes thereto.

11. Accounts Payable to Suppliers and Contractors

This item contains payables for the materials and services supplied to the Commission in the reporting year on the date set out in the statement.

12. Accounts Payable on Other Claims

	31.12.2007	31.12.2006
Due from the European Commission and the Ministry of Foreign Affairs of the Republic of Latvia to the Commission for business travel expense reimbursement	2 678	2 011
Other accounts payable to the Commission	335	188
	3 013	**2 199**

13. Settlements with the Administrators related to Guaranteed Compensation Payments

In order to protect the interests of the insured, by the 6 December 2002 Decision No. 322, On the Procedure for Making Payments from the Fund for the Protection of the Insured in the Case of *AK Alianse's* Bankruptcy, the Board of the Commission established the procedure for insurance indemnity payments. In protecting the interests of the insured, the insurance indemnity payments from the Fund for the Protection of the Insured in this company's bankruptcy makes up 8 607 lats (from 2003 to 2004), no payments were made from 2005 to 2007, consequently, accounting for the balance in the amount of 64 lats for unpaid insurance indemnities.

14. Staff Remuneration and Other Payments

This item contains remuneration to the staff of the Commission, including remuneration paid for specific work done for the Commission. Expenses related to remuneration to the Board comprised 16.05% of the total remuneration expenses (in 2005 – 15.1%). At the end of 2007, the Commission had 95 staff members (in 2006 - 94), and there were 96 positions at the Commission by the end of 2007 (in 2006 - 95).

	2007	**2006**
Staff remuneration, incl. members of the Consultative Council of the Financial and Capital Market	1 903 069	1 691 043
incl. remuneration to members of the Commission's Board	305 515	255 846
incl. remuneration to members of the Consultative Council of the Financial and Capital Market	4 060	4 460
Average number of employees per year	93	92
incl. the number of members of the Commission's Board	5	5
The number of members of the Consultative Council of the Financial and Capital Market	6	6

15. Staff Insurance

	2007	**2006**
Endowment life insurance	94 880	77 934
Health insurance	26 520	24 552
Accident insurance	2 847	3 682
	124 247	106 168

In accordance with the Procedure for Health Insurance, Accident Insurance and Endowment Life Insurance for the Commission's Staff, approved by the Board of the Commission, the Commission effected insurance for its staff, namely, endowment life insurance for those employees who had been employed by financial and capital market supervisory authorities for at least five years, as well as endowment life insurance for all employees of the Commission who performed the functions of state officials.

16. Improvements of professional skills and business trips

	2007	**2006**
Training and business trips abroad*	170 592	101 040
Professional training in Latvia	23 165	57 830
	193 757	**158 870**

* Incl. business travel expense reimbursement related to participation in the institutions of the European Union and other international organizations, 14 219 lats in 2007, while in 2006 - 21 084 lats.

Business trips included regular participation in the meetings of 50 EU institutions and their working groups, as well as meetings with financial supervision institutions in the US, Sweden, Estonia, Poland etc. and business trips for supervisory purposes to the subsidiaries of the Latvian financial and capital market participants in member states. Business trip share in total number of trips abroad comprised 70%.

17. Maintenance and General Service Expenses

	2007	**2006**
Rent of premises	216 495	176 847
Maintenance and public utility fees	35 823	23 180
Other maintenance and general service expenses	56 047	60 919
	308 365	**260 946**

A contract between the Commission and SIA Drave was concluded for the rent of premises at 1 Kungu Street, Riga, for 10 years, until 31 August 2011. An agreement was entered into on 18 September 2006 prescribing that as from 1 September 2006; the rent of the Commission's premises would be EUR 76 103 per quarter (EUR 304 412 per year or EUR 17.7 per square metre per month). On 18 October 2007, an agreement was entered into prescribing that as of 20 October 2007, the rent would be EUR 80 669 per quarter (EUR 322 676 per year or EUR 18.76 per square metre per month). The contract prescribes that the rent is revised and raised once a year in accordance with the consumer price index for the Republic of Latvia. Upon agreement in writing between the Commission and the lessor, the contract may be terminated before its expiry date. The Commission has no intention to terminate the contract.

[1] Consumer price index set by the Central Statistical Bureau of the Republic of Latvia.

18. Profesionālie pakalpojumi

	2007	2006
Compensation payments to administrators for financial and capital market participants in liquidation	37 796	1 121
Services in development of regulatory norms	27 140	-
The Commission's financial statements and quality management system audit	5 511	5 493
Lawyers services	2 360	-
Other professional services	9 258	13 509
	82 065	**20 123**

Other professional services covered expenses for translation, assessment of regulatory norms and provision of other specific professional services.

19. Court Proceedings and Claims

When performing functions specified by the Law on the Financial and Capital Market Commission, the Commission may become involved in court proceedings related to supervisory activities.

At the moment of signing the financial statements, the Commission, as a defendant, was involved in administrative proceedings, of which only in one application a claimant requested recovery of damages from the Commission: court proceedings were initiated on 17 May 2006, based on an application submitted by the joint stock Baltic International Bank to the District Administrative Court in respect of Decision No. 108 of the Commission's Board taken on 30 September 2005, under which the Commission rejected recovery of potential damages in the amount of 637 500 lats to the joint stock Baltic International Bank. The Board of the Commission is of the opinion that Decision No. 108 of the Commission's Board was passed justifiably and the application should be completely rejected. On 25 April 2007, the Court ruled in favour of the Commission. The Baltic International Bank lodged an appeal against the above court ruling. The Board of the Commission holds the view that the appeal court ruling will be also in favour of the Commission. The Commission therefore made no provisions for the said amount.

On 29 December 2006, an application was submitted to the District Administrative Court calling for revoking the 21 December 2006 Decision No. 215 of the Board of the Financial and Capital Market Commission on Withdrawal of the Credit Institution Licence Granted to the JSC OGRES KOMERCBANKA regarding the paragraphs on the withdrawal of the credit institution operating licence No. 06.01.02.01/104 granted to the JSC OGRES KOMERCBANKA and the Commission's application to the Riga Regional Court asking to put the JSC OGRES KOMERCBANKA into liquidation. In the said application to the court, the JSC OGRES KOMERCBANKA had neither claimed any damages from the Commission nor indicated the due amount of damages. Theoretically, in case of any administrative action there is an option to claim damages from an institution both by appealing the institution's administrative act to the court and by initiating separate proceedings. Up to now, the JSC OGRES KOMERCBANKA (in liquidation) has not made a claim for recovery of damages. The Board of the Commission holds the view that the JSC OGRES KOMERCBANKA cannot provide any material and legal basis to justify claiming recovery of any damages from the Commission. Justified and legal operations of the Commission have been also verified by the 2 February 2007 ruling of the Regional Administrative Court, according to which the claim from the JSC OGRES KOMERCBANKA against the Commission's decision was rejected. The Commission is of the opinion that the eventual court ruling also after adjudication the claim of the JSC OGRES KOMERCBANKA on its merits will be in favour of the Commission.

INDEPENDENT AUDITORS' REPORT

To the Parliament of the Republic of Latvia

Report on the Financial Statements

We have audited the accompanying financial statements of Financial and Capital Market Commission (hereinafter – the Commission) for the year ended 31 December 2007, set out on pages 18 through 32 which comprise the balance sheet as at 31 December 2007, the statements of income and expense, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

The Commission's management is responsible for the preparation and fair presentation of these financial statements in accordance with Cabinet Regulations No. 749 Procedure for Preparation of Annual Reports of State Institutions and Municipalities and the Commission's accounting policy disclosed in the Notes to these financial statements. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above give a true and fair view of the financial position of the Commission as at 31 December 2007, and of the results of their operations and their cash flows for the year then ended in accordance with Cabinet Regulations No. 749 Procedure for Preparation of Annual Reports of State Institutions and Municipalities and the Commission's accounting policy disclosed in the Notes to these financial statements.

Report on Compliance of the Management Report

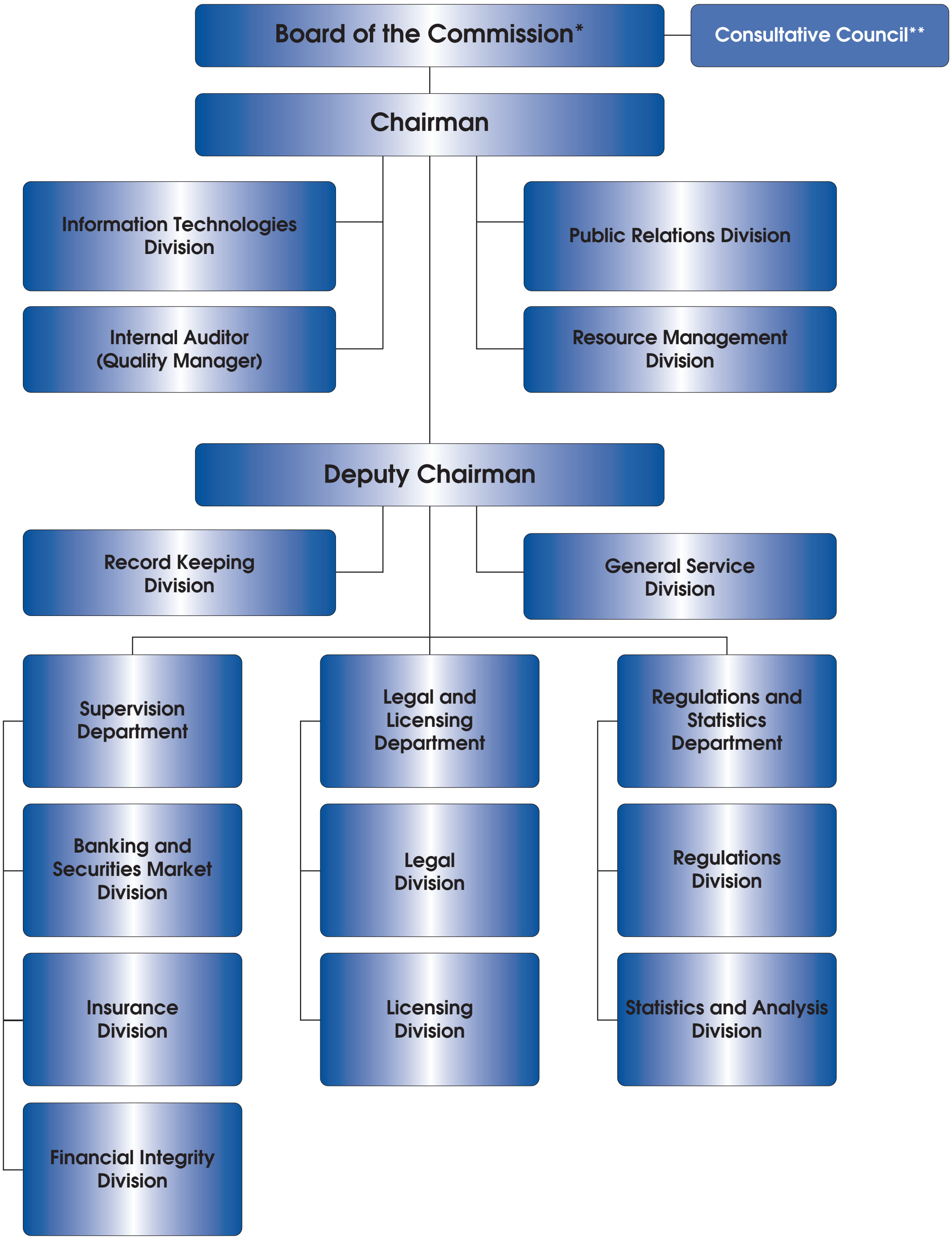
Furthermore, we have read the Management Report for the year ended 31 December 2007 (included on pages 3 through 4 of the accompanying 2007 annual report) and have not noted any material inconsistencies between the financial information included in it and the financial statements for the year ended 31 December 2007.

SIA Ernst & Young Baltic
Licence No. 17

Iveta Vimba
Personal ID code: 210275-12309
Member of the Board
Latvian Sworn Auditor
Certificate No. 153

Riga, 25 April 2008

STRUCTURE OF THE FINANCIAL AND CAPITAL MARKET COMMISSION



* The Board consists of five Board members: Chairman of the Commission, Deputy Chairman of the Commission and three Board members, who are simultaneously directors of the departments of the Commission.
** The Consultative Council of the Financial and Capital Market is formed on a parity basis from representatives of the Commission and heads of professional organisations of financial and capital market participants.

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A complete list of financial and capital market participants is available on the Internet home page of the Commission.