

**MEMORANDUM OF UNDERSTANDING  
BETWEEN THE BANK OF LATVIA AND THE BANK OF ESTONIA**

The Bank of Latvia (hereinafter: "the Latvian authority") and the Bank of Estonia (hereinafter: "the Estonian authority" and both hereinafter also referred to jointly as "the Latvian and Estonian authorities"),

**Referring** to the Basle Concordat and documents No. 30, "Core principles for effective banking supervision" and No. 27, "The Supervision of Cross-Border Banking" provided by Basle Committee on Banking Supervision (hereinafter: "Basle Documents"),

**Understanding** that no foreign banking establishment should escape from supervision and that the supervision should be adequate,

**Willing** to facilitate the performance of their respective duties and to promote the safe and sound functioning of cross-border credit institutions in their countries,

**Desiring** to promote and expand mutually beneficial co-operation and exchange of information between their countries on the basis of equality and non-discrimination,

**Convinced** that the exchange of information will contribute to increased mutual understanding and co-operation between the respective Latvian and Estonian authorities,

**Conscious** of the exchange of information being an essential element of the bilateral relationship between the Latvian and Estonian authorities,

**Having agreed** to supervise the credit institutions transacting cross-border business in Latvia and Estonia, as well as the financial institutions that are members of their respective consolidation groups, according to the legal framework applicable in Latvia and Estonia in the spirit of close collaboration and mutual trust,

The Latvian and Estonian authorities deem it necessary for the purpose of fruitful cooperation to create a common basis for finding practical arrangements for the procedures laid down in their legislation concerning the supervision of credit institutions and their cross-border establishments and to translate those arrangements into clear directions to their employees.

## **I GENERAL PROVISIONS**

### **- General framework**

By this Memorandum, the Latvian and Estonian authorities commit themselves to cooperate on a best-effort basis on all prudential matters pertaining to cross-border banking establishments

(hereinafter: "cross-border establishments"). For the purposes of this memorandum, the Latvian and Estonian authorities shall deem any branch, subsidiary, related company and representative office of credit institutions of both countries to be a cross-border establishment .

The Bank of Latvia shall supervise the activities of banks and other credit institutions that have been granted a license by the Bank of Latvia. The Bank of Latvia shall supervise and audit banks and other credit institutions and shall ensure that mandatory regulations issued by it are observed. A credit institution in the Republic of Latvia shall operate as a bank or as a credit union, or a branch of a foreign bank.

Banking Supervision in Estonia is carried out by the Banking Supervision Department of the Bank of Estonia. The supervision activities of the Banking Supervision cover the activity of all Estonian credit institutions and the subsidiaries, branches and representative offices of Estonian credit institutions in foreign states if they are not supervised by foreign supervisory authorities or if so agreed with foreign supervisory authorities. The subsidiaries, branches and representative offices of foreign credit institutions and companies belonging to the same consolidation group as the credit institutions will be supervised by the Estonian Banking Supervision unless otherwise agreed with the supervisory authorities of the relevant foreign states.

In Latvia the activities of cross-border establishments shall be governed by the laws of Latvia unless otherwise provided for in the international agreements concluded by Latvia. A foreign credit institution shall be obliged to respond to actions brought into Latvian courts and to comply with any decisions and orders of the Latvian authorities.

In Estonia the activities of cross-border establishments shall be governed by Estonian laws unless otherwise provided for in the international agreements concluded by Estonia. A foreign credit institution or financial institution shall be obliged to respond to actions brought into Estonian courts and to comply with any decisions and orders issued by the Estonian authorities.

## 2 - Form and extent of cooperation

### (i) Professional secrecy

Compliance with the obligation of professional secrecy by all employees receiving classified information in the course of their activities is absolutely necessary for successful cooperation between the Latvian and Estonian authorities.

Information received from either authority may be used for supervisory purposes only and shall be disclosed solely to the competent authorities provided for in the legislation of the country of the other authority. Beyond that it may not be given to third parties without the prior consent of the Latvian or Estonian authority, respectively.

### (ii) Exchange of information

The functions of the host country authority will include the duty of promptly informing the home country authority of any event of a cross-border establishment which comes to its knowledge and might jeopardize the stability of the credit institution as a whole. The Latvian and Estonian authorities recognise that according to the Basle Documents, the home country authority is entitled to gather information from cross-border banking establishments of banks or banking groups.

The Latvian and Estonian authorities will closely collaborate with each other both on a regular basis

and whenever a particular case so requires. Persons entrusted with home or host supervisory functions may at any time seek the advice of their peers from the other country. Whenever particular supervisory issues call for clarification, all available communication measures will be taken and *ad hoc* meetings may be arranged. Information visits will strengthen the mutual ties of cooperation.

The Latvian and Estonian authorities will notify each other of any substantial change in their domestic supervisory regimes and policies in general. They will inform each other of administrative penalties imposed or other actions taken on a cross-border establishment or institution as a whole if they consider such information to be of possible importance to the other authority.

In addition, the Latvian and Estonian authorities agree that home and host country authorities should inform each other upon request and to the extent reasonable on other prudential issues.

## **II ESTABLISHMENT OF A CROSS-BORDER ESTABLISHMENT**

### **- Licensing requirements**

In the spirit of the Basle Documents, the Latvian and Estonian authorities agree that consent for the creation of a cross-border establishment can be given by the host country authority only after it has been given by the home country authority. Particularly, there shall be prior consultation with the competent authorities of the other country involved on the authorization of a credit institution which is:

a subsidiary of a credit institution authorized in the other country, or  
a subsidiary of the parent undertaking of a credit institution authorized in the other country, or  
controlled by persons, whether natural or legal, who also control a credit institution authorized in the other country.

Before granting the authorization for a cross-border establishment, the home country authorities shall ensure that the credit institution fulfils adequate standards including the following:

fitness and properness of the management;  
accounting standards;  
requirements as regards internal controls;  
own funds;  
supervision of capital adequacy;  
supervision of risks arising out of open positions in markets;  
large exposures;  
qualifying holdings;  
owner control;  
all other requirements provided for in the domestic legislation.

The home country authorities shall inform the host country authorities concerning these issues.

The host country authorities, before granting the authorization, shall ensure that the home country authorities have given their consent for the cross-border establishments.

The home country authorities will see that a credit institution with several places of business established in the host country specifies one place of business as the head office, the managers of which are obliged to answer to the host country authorities.

The host country authorities shall have free discretion to require the head office to file a written notice of any place of business to be established in their territory.

#### Notices of change

In the event of a change in any of the particulars communicated pursuant to the programme of operations setting out, inter alia,

the types of business envisaged and the structural organization of a cross-border establishment,

the names of those responsible for the management of the cross-border establishment,

and the deposit-guarantee scheme which is intended to ensure the protection of depositors in the cross-border establishment,

the home country authority assures that the host country authority will be informed of the changes at least one month before making the change.

If the notice refers to a change in the management of the cross-border establishment, the Latvian and Estonian authorities will use the one-month interim period between the notice and the occurrence of the change to exchange information on the fitness and properness of the designated manager of the cross-border establishment.

### **III COOPERATION IN THE FIELD OF SUPERVISION**

#### - Cooperation in special fields of supervision

##### (i) Market Risks

The Latvian and Estonian authorities will consult each other regarding the prudential assessment of market risks if the situation in the financial markets of the host country gives rise to particular concern. They will inform each other on any crisis emerging with the potential to affect the domestic financial market as a whole (e.g., such as requiring the closing down of stock exchanges or a general moratorium on the banking industry), as soon as and to the extent legally possible.

The host country authority shall inform the home country authority of a cross-border establishment in breach of market rules if such information could be important to the home country authority. If necessary, the home country authority will inform the host country authority of any measures taken on the basis of such information.

Foreign exchange operations and positions of the cross-border establishment are on the joint responsibility of the home and host country authorities. In particular:

foreign exchange operations and positions of the branches are under the supervision of the home country authority;

foreign exchange operations and positions of subsidiaries are under the supervision of the authority of the country of incorporation on a solo basis and under the supervision of the home country authority on a consolidated basis.

## (ii) Liquidity

### a) Branches

The home country authority shall supervise the liquidity of the institution as a whole including its branches in the host country. The liquidity of a branch will be subject to host country supervision as well as to home country supervision.

The Latvian and Estonian authorities will examine regularly whether in their role as host supervisors they could avoid duplication of work in the area of liquidity supervision and restrict their activities in that field to the informing of the home supervisors as regards liquidity crunches emerging in their own financial markets.

If the branch fails to comply with the liquidity requirements of the host country, the following procedure shall be invoked:

The host country authorities will ask the credit institution to comply.

2. If the institution concerned fails to take the necessary measures to boost its liquidity to the legally required level, the host country authority shall inform the home country authority. The latter will take the necessary measures to induce compliance and shall communicate the nature of such measures to the host country authority.

3. If, however, the liquidity problem of the branch cannot be resolved, it shall be assumed that the credit institution faces a solvency problem, which is a matter to be handled by the home country authority.

Notwithstanding the aforesaid, the host country authorities will retain the power to take such measures as are necessary and appropriate in respect of the branch according to the respective legislation, and will keep the authorities of the home country informed of all activities.

### b) Subsidiaries

The primary responsibility to supervise liquidity rests with the authorities of the place of incorporation.

## (iii) Capital adequacy

### a) Branches

The primary responsibility to supervise capital adequacy rests with the home country authority. The host country authority has the general responsibility to monitor the financial soundness of foreign branches.

### b) Subsidiaries

Supervision of capital adequacy is a joint responsibility of both the host and home country authorities. The host country authority supervises the subsidiary as a separate entity and the home country authority on a consolidated basis.

## 2 - Reporting obligations; supervisory reporting

The host country will retain the right to impose reporting obligations on cross-border establishments, either in the interest of the general good or in those areas in which it retains supervisory control.

## 3 - Prevailing general law of the host country; code of conduct; priority of the general good

The supervision of a subsidiary shall remain within the jurisdiction of the country of incorporation. The authorities of the country of incorporation will be free to consult, whenever necessary, the supervisory authorities of the parent credit institution, which will to the extent reasonable provide the information requested to support the supervisory assessment of the condition of its subsidiary. In order to facilitate supervision on a consolidated basis, supervisory authorities of the parent credit institution shall have the same consultation and information rights.

The host country has the power to take appropriate measures to prevent or punish irregularities which are contrary to the legal rules it has adopted in the interest of the general good. This shall include the power to prevent offending institutions from initiating any further transactions within its territory.

If the activities of a cross-border establishment violate the legislation of the host country or offend against legislation, the host country shall proceed as follows:

1. The host country authorities point out the irregularity to the cross-border establishment, advise it of the legal situation and request compliance with the rules.
2. If the cross-border establishment does not comply with the request, the host country authorities will advise the home country authorities. The latter will take the necessary measures to have the cross-border establishment management meet the request and conduct its activities according to those rules.

Moreover, the host country will retain the power to prevent or punish a breach of law adopted in the interest of the general good within its territory.

## 4 - Bank customer complaints

Complaints about a particular cross-border establishment or credit institution providing services lodged by customers with the host country authorities will be handled by the latter on their own responsibility. They will be free to correspond directly with the cross-border establishment. They will, if necessary, pass on their findings to the home country authorities. The host country authorities are free to turn over to the home country authorities complex cases calling for the special expertise and knowledge of the latter.

Complaints lodged with the home country authorities will be handled by the latter. If the particular conditions in the host country are of relevance, the home country authorities will consult with the host country authorities, and eventually advise them of their decision.

## 5 - Crisis; bankruptcy; winding-up.

The Latvian and Estonian authorities will inform each other, without delay, if they become aware of a pending crisis concerning particular credit institutions with cross-border establishments in the other country or if the crisis is limited to the particular cross-border establishment.

In either case, the host country authority shall collaborate with the home country authority if supervisory countermeasures are to be taken by the latter. Moreover, the host country maintains the right to apply its own procedures concerning the winding up and reorganization of cross-border establishments that are on the verge of bankruptcy.

Before taking the actions stipulated in the national legislation against the cross-border establishment, the Latvian and Estonian authorities undertake to follow, when possible, the procedure agreed on in item III (3).

In serious cases the Latvian and Estonian authorities have the right to act immediately if necessary.

#### **IV COOPERATION IN THE FIELD OF ON-SITE INSPECTIONS**

The Latvian and Estonian authorities intend to carry out on-site inspections, either by their own staff or commissioned auditors. As host country authorities they do not intend to carry out on-site inspections on behalf of the home country authority. The host country authorities shall have the right to assist the inspector.

The Latvian and Estonian authorities will remain free to determine their own auditing standards and to appoint and assign commissioned auditors as well as their own staff of inspectors. Neither the host country authorities nor the involved credit institution may object to an inspection instituted by the home country authority.

The home country authorities shall notify in writing the host country authorities 15 days in advance of any inspection of a cross-border establishment instituted by themselves. The notification shall comprise the name of the inspector, name of the cross-border establishment, objective of the inspection, expected date of commencement and duration of the inspection.

In serious cases meetings may be arranged in the course of an inspection at the request of the inspector or either authority. Either authority may request a discussion of the findings.

The home country supervisory authority, upon completion of an on-site inspection in a cross-border establishment, shall notify the host country supervisory authority of the results. The Latvian and Estonian authorities shall inform each other of the results of the inspection in the form agreed upon separately.

#### **V COOPERATION CONCERNING OWNER CONTROL**

If any natural or legal person proposes to acquire, directly or indirectly, a qualifying holding in a credit institution authorized in the other country, there should be prior consultation between the Latvian and Estonian authorities.

If the acquirer of holdings referred to in paragraph 1 is a credit institution authorized in the other country or the parent undertaking of a credit institution authorized in the other country and if, as a result of that acquisition, the institution in which the acquirer proposes to acquire a holding becomes a subsidiary or subject to the control of the acquirer, the assessment of the acquisition must be subject to prior consultation with the competent authorities of the other country.

In this context a qualifying holding is defined as a direct or indirect holding in an undertaking which represents 10 per cent or more of the capital or the voting rights or which makes it possible to exercise significant influence over the management of the undertaking in which a holding exists. There must also be prior consultation between the Latvian and Estonian authorities if a natural or legal person as referred to in the previous paragraph proposes to increase his qualified holding so that the proportion of capital or the voting rights held by him would reach or exceed 20, 33 or 50 per cent or so that the credit institution would become his subsidiary. Also, the Latvian and Estonian authorities shall notify each other if the holder of a qualifying holding intends to reduce the holding below an extent described in previous sentence.

The Latvian and Estonian authorities shall provide each other with information upon request and to the extent reasonable of domestic enterprises which own one or more credit institutions incorporated in the other country. The information shall include all relevant facts pertaining to the shareholding enterprise itself and to the ownership structure as a whole.

## VI TECHNICAL ARRANGEMENTS

- Language; exchange of lists

Unless this memorandum or later agreements provide otherwise, the Latvian and Estonian authorities will correspond with each other in English. As regards meetings and other occasions, the language of use will be decided case by case.

The Latvian and Estonian authorities shall provide each other with a list of all those entities or individuals with whom in their countries incorporated credit institutions have "close links" either in the form of a list or a group organogram. The lists will be updated regularly.

The Latvian and Estonian authorities will also exchange lists of the following on a regular basis:

the credit institutions which they have authorized and which transact business within the territory of the other country through cross-border establishments; the lists should also include information concerning head offices as defined in Chapter 2 II and managers of the cross-border establishments;

the credit institutions which they have authorized and in which enterprises incorporated in the other country have direct holdings of more than 10%;

the cross-border establishments in their respective countries of credit institutions authorized in the other country;

the credit institutions, authorized by them, with representative offices in the other country and

the list of statistical reports by the Latvian and Estonian authorities.

The lists shall be updated at latest for the annual meeting.

### 2 - Exchange of staff

The Latvian and Estonian authorities will promote their mutual cooperation through visits for informational purposes and by arranging traineeships for each other's staff. If the duration of the



training period exceeds three months, the tasks of the trainee shall be as similar as possible to those performed by the staff of the authority arranging the traineeship.

- Regular meetings

The Latvian and Estonian authorities agree that it would be desirable to hold regular meetings in order to discuss the implementation of this memorandum and questions relating to the different credit institutions established in both countries and under their respective supervision and other relevant issues. The Latvian and Estonian authorities will aim to hold such a meeting once a year. The employees who have a part in the cooperation should convene once a year in such meetings to discuss fundamental issues so as to enhance the quality of cooperation. Such meetings shall provide a forum to analyse problematic cases, identify options and prepare proposals to the decision making bodies of the Latvian and Estonian authorities, and to settle disputes between them. Between such meetings ad-hoc meetings can be arranged as needed.

Mutual information on the following issues shall be updated at latest for the annual meeting:

substantial changes in the domestic country authority regimes and policies (legislation);

provisions upheld in the interest of the general good in the host country.

The Latvian and Estonian authorities hereby undertake to revise this memorandum of understanding in accordance with changes in national legislation or if the supervision of credit institutions so requires.

The Latvian and Estonian authorities agree to delegate the powers and rights of this Memorandum of Understanding to their successors, giving a written notice one month prior to the enforcement of the respective decision.

This memorandum of understanding was drafted on March, 7, 2000 in English.

On behalf of the Bank of Latvia

Einars Repše  
Governor  
Bank of Latvia



J. Cēbulis  
Latvijas Bankas  
reditestāžu uzraudzības pārvaldes  
iridiskās un licencēšanas daļas  
cencēšanas eksperts  
18.02.2000

J. Brizotova  
Latvijas Bankas  
Kreditestāžu uzraudzības pārvaldes  
vadītāja vietnieks juridiskajos un  
licencēšanas jautājumos  
21.02.2000

On behalf of the Bank of Estonia

Vahur Kraft  
Governor  
Bank of Estonia

Andres Trink  
Head of Banking Supervision Department

I. Lešinska  
Latvijas Bankas  
tulks redaktore  
28.02.2000

A. Šteinbergs  
Latvijas Bankas  
Kreditestāžu uzraudzības  
pārvaldes vadītājs

A. Sileniece  
Latvijas Bankas  
Galvenā grāmatvede

G. Vaitojevs  
Latvijas Bankas  
Ārējo sakaru pārvaldes  
vadītājs

I. Krastiņa  
Latvijas Bankas  
juriskonsulte  
25.02.2000