LATVIA

Diagnostic Review of Consumer Protection and Financial Capability

Volume II
Comparison against Good Practices

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Private and Financial Sector Development Department
Europe and Central Asia Region
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LATVIA

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Volume II
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Latvia: Summary of Financial Sector

Overview

The Latvian financial system had been growing rapidly before the global financial crisis hit. Total assets of the financial system rose at an average 33 percent rate from end-2003 to end-2008. As a result, the size of the financial sector as percent of GDP grew from 98 percent in 2003 to 162 percent in 2008. Banks led the growth with assets increasing from 89 percent of GDP in 2003 to 143 percent in 2008. Assets of leasing companies also increased significantly to reach 12 percent of GDP in 2008 (see Table 1).

Table 1: Structure of Latvian Financial System

<table>
<thead>
<tr>
<th>Institutions</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>Number of Institutions</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Assets (as percent of GDP)</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Banks</td>
<td>89.1</td>
<td>105.6</td>
<td>120.8</td>
<td>142.4</td>
<td>148.3</td>
<td>142.8</td>
<td>23 23 23 24 25 27</td>
</tr>
<tr>
<td>Commercial banks</td>
<td>85.3</td>
<td>100.2</td>
<td>114.4</td>
<td>133.7</td>
<td>136.6</td>
<td>126.4</td>
<td>22 22 22 21 21 21</td>
</tr>
<tr>
<td>Private</td>
<td>81.6</td>
<td>96.0</td>
<td>109.2</td>
<td>127.5</td>
<td>130.3</td>
<td>98.6</td>
<td>21 21 21 20 20 19</td>
</tr>
<tr>
<td>Foreign</td>
<td>40.3</td>
<td>45.9</td>
<td>60.9</td>
<td>80.8</td>
<td>82.9</td>
<td>72.2</td>
<td>9 8 8 9 10 10</td>
</tr>
<tr>
<td>Domestic</td>
<td>41.4</td>
<td>50.1</td>
<td>48.3</td>
<td>46.6</td>
<td>47.4</td>
<td>26.3</td>
<td>12 13 13 11 10 9</td>
</tr>
<tr>
<td>State-owned</td>
<td>3.7</td>
<td>4.3</td>
<td>5.2</td>
<td>6.2</td>
<td>6.3</td>
<td>27.8</td>
<td>1 1 1 1 1 2</td>
</tr>
<tr>
<td>Branches of foreign banks</td>
<td>4.1</td>
<td>5.4</td>
<td>6.4</td>
<td>8.7</td>
<td>11.7</td>
<td>16.4</td>
<td>1 1 1 3 4 6</td>
</tr>
<tr>
<td><strong>Nonbank financial entities</strong></td>
<td>9.0</td>
<td>10.1</td>
<td>12.2</td>
<td>14.3</td>
<td>18.2</td>
<td>18.9</td>
<td>108 116 116 126 127 134</td>
</tr>
<tr>
<td>Leasing companies</td>
<td>0.1</td>
<td>6.5</td>
<td>7.8</td>
<td>9.4</td>
<td>12.5</td>
<td>12.1</td>
<td>28 28 18 20 22 23</td>
</tr>
<tr>
<td>Credit unions</td>
<td>5.6</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>23 32 34 34 35 35</td>
</tr>
<tr>
<td>Electronic money institutions</td>
<td>-</td>
<td>-</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>- 2 3 6 7</td>
</tr>
<tr>
<td>Investment funds</td>
<td>0.4</td>
<td>0.5</td>
<td>0.8</td>
<td>1.0</td>
<td>1.3</td>
<td>0.8</td>
<td>16 15 17 21 34 38</td>
</tr>
<tr>
<td>Life insurance companies</td>
<td>0.5</td>
<td>0.4</td>
<td>0.4</td>
<td>0.5</td>
<td>0.4</td>
<td>0.4</td>
<td>6 5 5 5 4 4</td>
</tr>
<tr>
<td>Non-life insurance companies</td>
<td>1.7</td>
<td>1.7</td>
<td>1.7</td>
<td>1.7</td>
<td>1.8</td>
<td>2.0</td>
<td>13 12 12 11 11 11</td>
</tr>
<tr>
<td>State funded pensions</td>
<td>0.3</td>
<td>0.6</td>
<td>0.9</td>
<td>1.1</td>
<td>1.6</td>
<td>2.8</td>
<td>5 19 22 26 9 10</td>
</tr>
<tr>
<td>Private pension funds</td>
<td>0.4</td>
<td>0.4</td>
<td>0.4</td>
<td>0.5</td>
<td>0.5</td>
<td>0.5</td>
<td>17 5 6 6 6 6</td>
</tr>
<tr>
<td><strong>Total financial system</strong></td>
<td>98.4</td>
<td>115.7</td>
<td>133.0</td>
<td>156.7</td>
<td>166.5</td>
<td>161.7</td>
<td>131 139 139 150 152 161</td>
</tr>
</tbody>
</table>

Source: FCMC, Bank of Latvia, Central Statistical Bureau of Latvia

The size of the Latvian banking sector in relation to GDP is one of the highest in Eastern Europe. By end-2008, the share of Latvia’s banking sector assets in relation to GDP reached above 140 percent. This level was higher than that of Estonia (137 percent), Croatia (107 percent) and Hungary (101 percent) among other European countries (see Figure 1).
Market Infrastructure

At the same time, not all Latvians use formal financial services. It is estimated that only 64 percent of Latvians have an account with any financial intermediary. This is lower than Lithuania (70 percent) and Estonia (86 percent), as well as the average of western European states (91 percent). Despite the widespread increase in the use of financial services in Latvia, one third of the population still does not access the formal financial sector.

Table 2: Access to Financial Services

<table>
<thead>
<tr>
<th>% of Population</th>
</tr>
</thead>
<tbody>
<tr>
<td>Slovenia</td>
</tr>
<tr>
<td>Estonia</td>
</tr>
<tr>
<td>Slovakia</td>
</tr>
<tr>
<td>Lithuania</td>
</tr>
<tr>
<td>Russian Federation</td>
</tr>
<tr>
<td>Hungary</td>
</tr>
<tr>
<td>Poland</td>
</tr>
<tr>
<td><strong>Latvia</strong></td>
</tr>
<tr>
<td>Bulgaria</td>
</tr>
<tr>
<td>Kazakhstan</td>
</tr>
<tr>
<td>Croatia</td>
</tr>
<tr>
<td>Ukraine</td>
</tr>
<tr>
<td>Romania</td>
</tr>
<tr>
<td>Average Western Europe</td>
</tr>
</tbody>
</table>

Note: Data as of December 2007
Source: World Bank

Latvia’s credit reporting system is in its early stages of development. The public credit registry covers only some 4 percent of the adult population. The extent of the coverage falls significantly below the average of other European countries, including Estonia and Lithuania (see Figure 1). The weak coverage of the credit reporting system is likely resulting in increased borrowing costs for households with borrowers paying a significant credit risk premium.
The process for enforcing collateral is short and quick but not inexpensive. Latvia is ranked eleventh in terms of countries with the fewest number of procedures and 20th in estimated number of days required to enforce contracts (see Table 3). Speedy enforcement of liens on collateral provides lenders with the reassurance that they are able to fully rely on the collateral they are taking for their loans. In terms of cost of enforcement, Latvia is ranked 63rd with an average cost of 23 percent of a claim. The cost is slightly below the average of Central and Eastern Europe (26 percent).

Table 3: Efficiency of Systems for Enforcing Contracts in Europe

<table>
<thead>
<tr>
<th>Country</th>
<th>Number of Procedures</th>
<th>Number of Days</th>
<th>Cost (as % of Claim)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Belgium</td>
<td>25</td>
<td>505</td>
<td>16.6</td>
</tr>
<tr>
<td>Latvia</td>
<td>27</td>
<td>309</td>
<td>23.1</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>27</td>
<td>611</td>
<td>33</td>
</tr>
<tr>
<td>New Zealand</td>
<td>30</td>
<td>216</td>
<td>22.4</td>
</tr>
<tr>
<td>Lithuania</td>
<td>30</td>
<td>275</td>
<td>23.6</td>
</tr>
<tr>
<td>Germany</td>
<td>30</td>
<td>394</td>
<td>14.4</td>
</tr>
<tr>
<td>Slovakia</td>
<td>30</td>
<td>565</td>
<td>30</td>
</tr>
<tr>
<td>Romania</td>
<td>31</td>
<td>512</td>
<td>28.9</td>
</tr>
<tr>
<td>Estonia</td>
<td>36</td>
<td>425</td>
<td>26.3</td>
</tr>
<tr>
<td>Russia</td>
<td>37</td>
<td>281</td>
<td>13.4</td>
</tr>
<tr>
<td>Poland</td>
<td>38</td>
<td>830</td>
<td>12</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>39</td>
<td>564</td>
<td>23.8</td>
</tr>
</tbody>
</table>

Central and Eastern Europe | 37.1 | 450.9 | 25.6 |

Source: World Bank, *Doing Business 2008*
Latvia: Consumer Protection in the Banking Sector

Overview

The Latvian banking sector is moderately concentrated and mostly foreign-owned. The banking concentration in terms of assets has been growing in the past four years. The market share of the five largest banks increased from 62 percent by end-2004 to 69 percent by end-2008. The participation of domestic capital in the equity of the banking system has decreased from 41 percent in 2005 to 31 percent in 2006 and around 22 percent in 2007 and 2008 (see Figure 1).

![Figure 3: Share Capital of the Latvian Banking System by Country](source)

The rapid expansion of the banking sector was driven by lending to households. The banking sector loan portfolio grew at an average annual rate of 50 percent from 2004 to 2007. During the same period, loans to the household sector increased 70 percent on average per year, a much higher rate than that of loans to the private non-financial sector (45 percent on average). Starting from 2008, the rate of growth in the banking sector has been slowing down significantly. By June 2009, the year-to-year growth rate of total banking loans was only 0.23 percent, and loans to households experienced a yearly decrease of 0.72 percent.

![Figure 4: Year-to-Year Growth of Banking Sector Loans](source)
Loans for housing purchases have led the expansion of household loans. From 2004 to mid-2007, loans for housing purchases have experienced yearly growth rates above 80 percent. Their share in the household loan portfolio increased from 68 percent in December 2004 to 79 percent in June 2007, and their size, relative to GDP, increased from 12 percent by end-2004 to 32 percent by end-2007.

Household borrowings in foreign currency have significantly increased, particularly for housing purchases. The share of foreign currency loans in the household loan portfolio has increased from 70 percent in 2005 to 88 percent in 2008. This growth has been driven by loans for housing purchases and other household loans. The share of foreign currency exposure in consumer credits has decreased from 44 percent in 2005 to 35 percent in 2008. Loans for housing purchase in foreign currency represented 30 percent of GDP by end-2008 (vs. 14 percent by end-2005). Above 96 percent of loans in foreign currency have been extended in Euros.

Table 4: Share of Foreign Currency Loans
(in percentage)

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>Private non-financial sector</td>
<td>69.3</td>
<td>76.8</td>
<td>87.2</td>
<td>89.9</td>
</tr>
<tr>
<td>Household sector</td>
<td>69.7</td>
<td>77.2</td>
<td>85.9</td>
<td>87.5</td>
</tr>
<tr>
<td>Housing purchases</td>
<td>72.7</td>
<td>81.2</td>
<td>92.4</td>
<td>95.0</td>
</tr>
<tr>
<td>Consumer credit</td>
<td>43.7</td>
<td>46.5</td>
<td>37.8</td>
<td>34.9</td>
</tr>
<tr>
<td>Other loans to households</td>
<td>82.4</td>
<td>88.3</td>
<td>93.3</td>
<td>95.2</td>
</tr>
</tbody>
</table>

Source: FCMC
Legal Framework and Institutional Arrangements

The main laws and regulations providing for consumer protection in the banking sector are the following:

- Civil Code
- Criminal Code
- Administrative Procedure Law
- Consumer Rights Protection Law (March 1999, as last amended in June 2009)
- Unfair Commercial Practices Prohibition Law (January 2008)
- Advertising Law (January 2000, as last amended in December 2007)
- Credit Institutions Law (effective 1 January 2007, as last amended in February 2007)
- Regulations regarding Consumer Credit Agreements, Cabinet Regulation No. 692 (25 August 2008)
- By-law of the Consumer Rights Protection Centre, Cabinet Regulation No. 632 (1 August 2006)
- Deposit Guarantee Law
- Procedures for the Submission and Examination of Consumer Claims regarding the Non-conformity of Goods or Services with Contract Provisions Issued pursuant to Section 27, Paragraph three of the Consumer Rights Protection Law, Cabinet Regulation No. 631 (1 August 2006)
- Law on Submission (September 2007)
- Financial Collateral Law

The Financial and Capital Market Commission (FCMC) licenses banks, insurance companies and other financial institutions, and is in charge of the prudential supervision of their activities. The FCMC is responsible for ensuring stability, and free competition within the financial and capital markets. The FCMC has also the authority to impose penalties upon the participants in the financial and capital market and their officials if regulatory requirements are violated.

The Consumer Rights Protection Centre (CRPC) is a “direct administration institution” supervised by the Ministry of Economics, which reports to the Competition, Trade and Consumer Rights Division of the Department of Internal Markets of the Ministry of Economics. The CRPC is responsible for implementing the protection of consumer rights and interests, and conducting market supervision in the field of consumer protection regarding all types of goods and services, including financial services.

The Association of Latvian Commercial Banks was founded on July 23, 1992 and has 23 members as of June 2009. The Association has developed the Banks’ Code of Conduct and has developed an Arbitration Court. The Association also has set up an Ombudsman, but only in respect of credit transfers or transactions effected by an electronic payments system.
## Good Practices: Banking Sector

### SECTION A  CONSUMER PROTECTION INSTITUTIONS

<table>
<thead>
<tr>
<th>Good Practice A.1</th>
<th>Consumer Protection Regime</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>The law should provide for clear consumer protection rules regarding any regulated financial product or service, and all institutional arrangements should be in place to ensure the thorough, objective, timely and fair implementation and enforcement of all such rules.</td>
</tr>
<tr>
<td></td>
<td><strong>a.</strong> Specific statutory provisions need to create an effective regime for the protection of any consumer of a banking product or service.</td>
</tr>
<tr>
<td></td>
<td><strong>b.</strong> Either a general consumer agency or a specialized agency should be responsible for implementing, overseeing and enforcing consumer protection, as well as collecting and analyzing data (including complaints, disputes and inquiries).</td>
</tr>
<tr>
<td></td>
<td><strong>c.</strong> The law should provide and not prohibit a role for the private sector, including voluntary consumer protection organizations and self-regulatory organizations, regarding consumer protection in general and in financial products and services in particular.</td>
</tr>
</tbody>
</table>

### Description

The first Latvian Consumer Rights Protection Law was enacted in 1992, within a year after the restoration of the country’s Independence on September 6, 1991. Concerted policy-making in the field of consumer protection was, however, initiated as of 1995 when Latvia first applied for membership of the European Union (EU). Concluding an association agreement with the EU, Latvia then undertook to promote and ensure a consumer protection policy that was in line with EU laws, as well as the United Nations’ 1986 guiding principles for consumer protection. Latvia also agreed to adjust its consumer protection policies and laws in accordance with the EU Directives and Regulations. However, EU Directives are mostly based on minimum harmonization. Thus, some Latvian Consumer Rights Protection Laws and regulations provide higher level of protection than that required by EU Directives.

By the terms of Latvia’s Consumer Rights Protection Law adopted in 1999, consumer protection rules are provided in respect of any financial product or service, whether regulated or not. The purpose of this Law is, in part, “to ensure that consumers are able to exercise and protect their lawful rights when entering into contracts with ... service providers.”

In line with EU Council Directive 93/13/EEC, the Consumer Rights Protection Law defines a consumer as “a natural person who expresses a wish to purchase, purchases or might purchase goods or utilizes a service for a purpose, which is not related to his or her economic or professional activity”. Defined as “a person who within the scope of his or her economic or professional activity provides a service to a consumer”, the term “service provider” covers all institutions providing financial services to consumers, including commercial banks, non-bank credit institutions, securities, insurance companies and private pension funds.

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1. Law on Consumer Rights Protection 1992
3. The Consumer Rights Protection Law adopted in March 1999 has most recently been amended with effect from 23 June 2009.
4. See Section 2 of the Consumer Rights Protection Law
5. Article 2(b) of the EU Council Directive 93/13/EEC of 5 April 1993 on Unfair Terms in Consumer Contracts defines “consumer” as “any natural person who, in contracts covered by this Directive, is acting for purposes which are outside his trade, business or profession.”
6. See Section 1 of the Consumer Rights Protection Law.
Specific, detailed provisions deal with the protection of any consumer obtaining consumer credit, entering into a distance contract and other matters of relevance to the banking industry.

The **Unfair Commercial Practices Prohibition Law**\(^7\) builds directly upon the Consumer Rights Protection Law and expressly adopts the same defined terms, including those of “consumer” and “service provider”. The purpose of the Unfair Commercial Practices Prohibition Law is to ensure “the protection of the rights and economic interests of consumers by prohibiting performers of commercial practices from utilizing unfair business-to-consumer commercial practices”.\(^8\) Once again, this law covers the commercial practices of all institutions providing financial services to Latvian consumers.

The **Advertising Law**\(^9\) is also relevant. Its purposes are expressly:

a) to regulate the production and dissemination of advertising, as well as to determine the rights, obligations and liabilities of persons involved in the production and dissemination of advertising;

b) to protect the interests of persons as well as the general public in the field of advertising; and

c) to promote fair competition.

In addition, as is indicated below, there are numerous provisions of the Latvian Civil Code which have a direct bearing on matters of consumer protection in financial services.

Finally, it is essential to note the **Regulation regarding Consumer Credit Agreements**\(^10\) which prescribes the information to be included in any consumer credit agreement, the conditions when these requirements do not apply, how the annual interest rate is properly calculated, as well as the basis on which 'equitable reduction' in the total cost of credit is permissible. It is worth noting that the Regulation is also applicable to mortgage loan agreements. The Regulation is thus super-equivalent in the sense that its scope is broader than the EU Consumer Credit Directive, which applies to non-secured transactions of between 200 and 75,000 Euro.\(^11\)

Although other laws and regulations also have bearing on consumer protection in financial services, new laws and amendments to existing laws are required to fill gaps and correct anomalies in the present framework. Apart from the suggestions for specific legislative amendments appearing below, an overhaul of the statutory provisions dealing with consumer dispute resolution and the enactment of a law on debt collection operations are recommended.

The Consumer Rights Protection Law, the Unfair Commercial Practices Prohibition Law, the Advertising Law and the Regulation regarding Consumer Credit Agreements are each applied and enforced by the **Consumer Rights Protection Centre** (CRPC) established in 1998.\(^12\)

The CRPC is a “direct administration institution” supervised by the Ministry of Economics, which reports to the Competition, Trade and Consumer Rights Division of the Department of Internal Markets of the Ministry of Economics. The CRPC is responsible for implementing the protection of consumer rights and interests, and conducting market supervision in the field of consumer protection regarding all types of goods and services, including financial services.

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\(^{7}\) In force as of 1 January 2008.

\(^{8}\) Section 2 of the Unfair Commercial Practices Prohibition Law.

\(^{9}\) Originally enacted in January 2000, and last amended in December 2007.

\(^{10}\) Cabinet Regulation No. 692 adopted 25 August 2008 and in force as of 1 September 2008.


\(^{12}\) Although the applicable provisions of the Civil Code must, of course, be considered and accepted in any deliberations of the CRPC, it falls to the Civil Divisions of Latvia’s Courts (and not the CRPC) to ensure the application and enforcement of Civil Code requirements.
By the terms of the Consumer Rights Protection Law, the CRPC is a “direct administration institution” subject to the control of the Ministry of Economics. The Director of the CRPC is appointed to, and released from, office by Cabinet on the recommendation of the Minister of Economics.

The purpose of the CRPC is to ensure the effective protection of consumer rights and interests. The main functions of the CRPC include (responsibilities regarding financial services are highlighted):

1. monitoring and controlling the trade of non-food products (except medical products, medicinal products, veterinary medicinal products, pharmaceutical products, cosmetics, veterinary pharmaceutical products, animal care products, household chemical substances and chemical products) and the provision of services;
2. specifying the correct determination of the weights and measures of food and non-food products, as well as the supervision of correct calculation of payment for purchases;
3. organizing and coordinating the co-operation of non-government organizations for consumer rights protection and of the other supervisory and monitoring institutions for consumer rights protection involved in implementation of State policy;
4. examining submissions of consumers regarding violations of consumer rights, providing assistance to consumers in resolving conflicts with respect to manufacturers, sellers or service providers, as well as requiring compliance with the lawful claims of consumers;
5. providing legal assistance to consumers regarding issues of consumer rights protection;
6. supervising compliance with consumer rights regarding draft contracts and contracts entered into between consumers and manufacturers, sellers or service providers, as well as the performance of activities provided for in regulatory enactments in order that the manufacturer, seller or service provider makes changes in draft contracts or discontinues the performance of the contract terms if unfair or ambiguous contract provisions are determined in the draft contract;
7. supervising compliance with the Unfair Commercial Practices Prohibition Law and the Advertising Law; and
8. performing functions specified in other laws and regulatory enactments.

With limited resources at its disposal and lack of specialists in financial services, the CRPC is hard pressed to respond to consumer inquiries, complaints and disputes regarding financial issues, let alone to carry out significant business-conduct supervisory functions regarding banks and other financial institutions.

In addition, the CRPC has yet to collect and analyze data (including consumer complaints, disputes and inquiries) in a systematic way.

The Financial and Capital Market Commission (FCMC) licenses banks, insurance companies and other financial institutions, and is in charge of the prudential supervision of

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13 Detailed provisions regarding the competence, functions and tasks of the CRPC, the role of officials of the CRPC and reports on its activities are found in the By-law of the Consumer Rights Protection Centre, Cabinet Regulation No. 632 of 1 August 2006.
14 From Section 25 of the Consumer Rights Protection Law
15 The apparent consequences for any failure by Centre staff to act as required seem potentially harsh. By Section 319 (1) of Latvia’s Criminal Code, if a State official fails, whether intentionally or through negligence, to perform his or her duties as provided by law, and substantial harm is caused thereby to any right or interest of a person (as protected by law), that official, on conviction, is subject to imprisonment for a term not exceeding three years, or custodial arrest, or community service, or a fine not exceeding fifty times the minimum monthly wage, with or without deprivation of the right occupy specified positions for a term of not less than one and not exceeding three years.
their activities. Unlike the CRPC, the FCMC is an independent public authority that reports directly to the Parliament. Also, it is well-funded to perform its tasks.

The FCMC is responsible for ensuring stability, and free competition within the financial and capital markets. The FCMC has also the authority to impose penalties upon the participants in the financial and capital market and their officials if regulatory requirements are violated.

As far as private sector involvement in consumer protection is concerned, the law expressly provides that consumers are entitled to unite voluntarily in associations aimed at protecting consumer rights. The sole proviso is that all such organizations and associations act in accordance with regulatory enactments, as well as their own articles of association.\textsuperscript{16}

Associations devoted to consumer rights protection have the right:
1) to participate, together with the CRPC, in inspections related to compliance with quality requirements of services to be provided;
2) to examine complaints and proposals of consumers, and to provide necessary assistance to consumers in cases where their rights have been violated;
3) to submit statements of claim to a court regarding the protection of consumer rights and interests, and to represent the interests of consumers in court;
4) to purchase products and order services in order to perform comparative examinations of products and services; and
5) to submit proposals to the CRPC for the performance of activities if a violation of consumer rights has allegedly occurred which affects the interest of an individual consumer or a group of consumers (including those of consumer associations) and which may have a negative impact on particular consumer rights.\textsuperscript{17}

The CRPC is entitled to establish a consultative council, including representatives of State institutions, consumer rights protection associations, and service provider organizations.\textsuperscript{18} More is needed, however, to make this Council a functioning, effective reality.

The NGO community is woefully lacking in resources, with the result that these rights are rarely exercised.

There are two main bodies representing the rights and interests of consumers of financial services. The first and most established is the Club for Protection of Consumer Interests.\textsuperscript{19} It was created in 1990 and covers the full range of services and products available to consumers. It has extremely limited capacity and does not have expertise in financial services.

A second institution which has been established more recently is the Latvian Borrower’s Association\textsuperscript{20}. It is a small association that started representing the rights of around 1,000 borrowers, although new members are joining regularly. Membership is set at LVL 12 and gives access to an advocacy service and legal consultations. The Association is staffed largely by volunteers who give their time for free.

\textbf{Recommendations}

Consideration should be given to:

a) improving the legal framework for dispute resolution\textsuperscript{21} and drafting a law on debt collection, as well as other matters referred to in separate sections below;

b) strengthening the institutional framework for financial consumer protection by one of the following options:

- establishing a separate Unit within the CRPC devoted exclusively to financial services issues, and providing independence and status to the CRPC as the

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\textsuperscript{16} From Section 22 of the Consumer Rights Protection Law
\textsuperscript{17} See Section 23 of the Consumer Rights Protection Law
\textsuperscript{18} Section 25(12) of the Consumer Rights Protection Law
\textsuperscript{19} See http://www.consumer-guide.lv/english/club.htm
\textsuperscript{20} See http://www.kreditnemeji.lv/
\textsuperscript{21} For a discussion of Formal Dispute Settlement Mechanisms, see Good Practice E. 2 below.
business conduct regulator in financial services, in line with what has been provided to the FCMC as prudential market regulator;

- expanding the role of FCMC regarding financial consumer protection while leaving resolution of consumer financial disputes to the CRPC;

- creating a new financial consumer protection agency, with jurisdiction and staff focused exclusively on consumer protection in financial services and with independence and a status equivalent to the FCMC so that oversight of business conduct in the provision of financial services to consumers is carried out effectively, including the control of abusive lending practices;

- setting up a special agency, such as a financial ombudsman, to handle financial consumer inquiries, complaints and disputes

  c) funding the CRPC or any other agency dealing with financial consumer protection, at least in significant part from the financial services industry so that qualified banking, legal and other professionals can be employed;

  d) requiring all relevant institutions, including the CRPC, the Association of Latvian Commercial Banks and consumer NGOs to meet regularly in an effective consultative council in order to address and solve issues of consumer protection in financial services in general and banking services in particular in a coordinated fashion;

  e) improving the transparency, availability and quality of data of relevance to consumer protection in financial services, including consumer complaints and their treatment, as well as relevant recommendations made, and decisions taken, by the CRPC; and

  f) seeking additional funding for the NGO community.

<table>
<thead>
<tr>
<th>Good Practice A.2</th>
<th>Codes of Conduct for Banks</th>
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<tbody>
<tr>
<td>a.</td>
<td>There should be a principles-based, statutory code of conduct for banks that is devised in consultation with the banking industry and if possible with consumer protection associations, and is monitored by a statutory agency or an effective self-regulatory agency.</td>
</tr>
<tr>
<td>b.</td>
<td>Every bank, acting alone and together, should publicize and disseminate this statutory code of conduct to the general public through appropriate means.</td>
</tr>
<tr>
<td>c.</td>
<td>The statutory code should be augmented by voluntary codes of conduct for banks on such matters as facilitating the easy switching of consumers' current accounts and establishing a common terminology in the banking industry for the description of banks' charges, services and products.</td>
</tr>
</tbody>
</table>

| Description        | There is no statutory code of conduct for Latvian banks. |

Since January 1, 2008, however, the Unfair Commercial Practices Prohibition Law has expressly provided that in order to promote the protection of consumer rights and economic interests and the observance of the law, performers of economic or professional activity (e.g. banks, non-bank credit institutions, and other financial service providers) or professional associations (e.g. the Association of Latvian Commercial Banks) may (emphasis added) develop a "good practice code". By the terms of the Law, any such code constitutes a voluntary agreement of the "performers of an economic or professional activity" and "in respect of matters not regulated by law". Nevertheless, any such code would "regulate the behavior of [the] performers of commercial practices who have

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22 This means increasing the allocations made to the CRPC in the 2008-2010 Consumer Protection and Market Surveillance Program and obtaining important additional funding from the industry, as well as the EU and donors.

23 Ibid.

24 Ibid.

25 See Section 5 (1) of the Unfair Commercial Practices Prohibition Law.
undertaken to fulfill the commitments specified in the good practice code in one or several types of commercial practices, as well as in one or several fields of economic or professional activity. Thus, provided, for example, that some or all banks were actually to undertake to abide by a Code of Conduct, supervising the proper application by these banks of their Code provisions would implicitly become the responsibility not only of each bank but also of the CRPC. In preparing a good practice code, guidelines of fair commercial practice and professional diligence criteria may be included, but these must conform to generally recognized fair market practices and to the principle of good faith in the relevant field of economic or professional activity. Although not explicitly stated in the Law, any Code obviously must, in addition, conform strictly with the law.

As elaborated under B.5 below, a commercial practice is regarded as misleading, if, among other things, the performer of the practice (e.g. a bank) has agreed to a Code of Conduct and then does not observe its “obligations” in these respects. By expressing agreement with a Code of Conduct, the Unfair Commercial Practices Prohibition Law seems to remove the voluntary nature of adherence to a Code’s “requirements”. By statute, express agreement with the provisions of a Code of Conduct is apparently tantamount to an undertaking faithfully to fulfill all Code provisions and a willingness to be bound by them. Query, however, what constitutes “agreement” in these respects. It would seem that an authorized signature on behalf of the “performer of the practice” would be needed (i.e. something more than the issuance of a Code of Conduct by a General Meeting of a Members’ Association), but this is not clear.

The latest “principles-based” Code of Conduct for commercial banks was generated within the Association of Latvian Commercial Banks and approved by its General Meeting of Members on February 28, 2003. By the terms of the 3rd paragraph of the Preamble to the Banks’ Code of Conduct: “The Code is of recommendatory nature. The Association of Latvian Commercial Banks [simply] appeals to all banks to apply this Code in their practical operations.”

The Banks’ Code of Conduct summarizes banking standards and practices for the purpose of promoting “understanding and trust as regards banks’ interrelations [as well as] bank and customer relations”. The 2nd paragraph of the Preamble states the hope that the Code “may serve banks’ customers to better understand the way an individual bank should organize relations with clients.” It is also expressly stated that the Code shall be “modified on a regular basis, in order to comply with changes in banks’ operations”.

As an essential underlying principle, banks are encouraged to “ensure that information on the banks’ services is true and publicly available.” Banks also should “not support any actions directed towards the restriction of competition and ... [must] comply with the principle of fair competition”. In their advertisements, public releases, comments and any publications, “banks shall only use true information.” Banks are also encouraged to “carefully choose and supervise their personnel, as well as ... regularly upgrade its qualification.” In addition, banks should “keep confidential personal, account, deposit and business secrets, unless laws and regulations provide for otherwise”. And, “at the time of
providing their services, bank personnel shall comply with the legal interests of all parties". 38
So-called "customer services sites" are to make "information on essential bank services, regulations and prices ... freely available". 39 And, "at the time of opening an account in the customer's name, banks [are to] provide the client with all required information on performance of banking services". 40 Also, if clients are financially sophisticated enough to request more, "banks shall also provide customers with 'relevant' additional information", it implicitly being for the bank to decide what is "relevant". 41 In addition, banks are admonished to "provide new customers with a written summary or explanation of the essential features of offered services". 42 Banks are also to "counsel customers on the regulations of provided services, including the provision of comprehensive and honest information of possible risks". 43 And, the relationship between a bank and its customer must be one "based on a written agreement [... that is] unambiguous and clear ... [and] sets forth the rights and obligations of both parties ... taking into account both the bank's and the customer's interests". 44

It would seem, though, that all of these words are of grand intentions, having little or no meaning in practical terms. In the first place, the Code appears not to have been formally endorsed by any bank and its provisions are apparently neither internalized nor applied by any bank. Without signing the document 45 or in some other way formally accepting its provisions, it appears difficult to argue that any member bank in February 2003 can be taken to have agreed with this Code. As a result, it would seem that no bank has left itself open to the possibility that it might be accountable to consumers, the CRPC and the Association for the faithful application of the Code in its day-to-day operations. Secondly, the Code is not publicized or disseminated, whether by banks or the Association, on websites or otherwise. And thus, contrary to the first clause of its Preamble, the Code does not, and cannot possibly, provide a consumer with any understanding of the way a bank should organize its consumer relations.

Turning to various Articles of the Code, apparently few banks, among other things, provide "customer service sites" at which information on essential bank services, regulations and prices is freely available. Also, although banks not surprisingly as a general rule, do provide their clients certain information at the time of opening an account, the Code provides no objective rules in these respects. Rather the Code allows banks to decide themselves whether they provide amounts to "all [that is] required ... on performance of banking services". In addition, the level of exposure of consumers to interest and foreign exchange risks raises doubt about the disclosure by banks of comprehensive information on possible risks faced by consumers.

As the drafters of the Code made clear, their purpose was to offer guidance only. But, as indicated, this guide appears rarely, if ever, to have been followed. Also, so far at least, the provisions of the Unfair Commercial Practices Prohibition Law implying an undertaking by individual banks to fulfill the terms of the Code have not taken effect and the extent to which any Code "requirement" is applied by individual banks is in no way monitored by the banking association, the CRPC or any other agency. Although the banking association does sponsor worthwhile activities, including a certificate training program for senior bankers, it would be wrong to describe the association as even pretending to be an "effective self-regulatory agency" in these or any other respects.

Following the enactment of the Unfair Commercial Practices Prohibition Law, the February 2003 Code has in some respects been made less relevant. And, notwithstanding the last

38 Article V (2)
39 Article VII (1)
40 Article VII (2)
41 Ibid
42 Article XII (2)
43 Article VII (3)
44 Article X
45 By the terms of Section 11 1) of the Unfair Commercial Practices Prohibition Law, a hint at least is provided that the signing of the Code of Conduct by the service provider is a prior requirement.
paragraph of its Preamble which states that "[t]he Code shall be further modified on a regular basis, in order to comply with changes in banks' operations," there does not appear to be any on-going attempt within the banking association to draft a wholly revised and updated version of the Code for wide, formal adoption by member banks.

Finally, some banks do make reference on their websites to their own Codes of Ethics but none of these are anything more than statements of good intentions. They do not create obligations for any bank.  

In the specific case of mortgages, two banks have signed the European Code of Conduct on Home Loans, although implementation is not scheduled until later this year for one and 2010 for the other. It would be relatively straightforward to implement this Code of Conduct across the banking sector, given that all the Nordic banks already implement the Code in their own countries.

**Recommendations**

The Association of Latvian Commercial Banks should be encouraged to draft a revised and updated Code of Conduct for formal endorsement by all member banks. Among other things, consideration should be given to having this new Code:

- facilitate the easy switching of consumers' current accounts;
- establish a common terminology in the banking industry for the description of banks' charges, services and products;
- set minimum standards regarding the information to be provided in any advertisement;
- deal with the prevention of conflicts-of-interests;
- establish uniform standards in respect of various matters, including the marketing and advertising of services, the handling of delinquent debt, and the training of a lender's employees;
- deal with the consideration of inquiries and the procedures regarding claims, including required efforts to reach pre-trial amicable resolution of disputes and clearly structured options for any consumer who complains to his or her banker after all voluntary means of settlement have proven futile, including, in particular, the process of initiating action in the CRPC, the courts or a possible future financial consumer protection agency or financial ombudsman;
- provide for measures needed to improve a lender's services, as well as the Code of Conduct;
- deal with how a failure to observe any norm of the Code would be established;
- deal with the consequences of any such failure; and
- provide for how the Code must be published and disseminated.

This should ideally be more than a description of what, ideally, should happen. It should rather be a plan to make things happen.

Consideration might also be given to establishing a principles-based, **statutory** code of conduct for banks that is devised either by an enhanced CRPC or a new agency in close consultation with the Association of Latvian Commercial Banks, individual banks and consumer protection associations. Once enacted, this would then need to be strictly monitored to ensure compliance with the law.

Minimum standards for banks need to be clearly agreed, articulated and applied in order to limit the risk of negative experiences with unethical behavior eroding consumer confidence in the entire market. Such standards will also improve the competitive climate between banks, for instance by reducing misleading information given to consumers about a bank's products or the products of its competitors.

The power of dialogue should not be underestimated, initially between banks, but then, as discussion develops, between banks and consumer groups and government. As European experience has demonstrated, consensus stemming from dialogue about consumer

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46 See, for example, the websites of SGB Baltics and of Parex Banka.
An updated Code of Conduct (whether in place voluntarily or by statute) that is widely disseminated, generally understood and enthusiastically applied would bring many advantages to banks and consumers. On the one hand, customers would be assured that banks could not violate essential principles without facing consequences. On the other hand, the “best” banks in these respects would quickly stand out and presumably benefit from greater business as a result. Although a series of what might be termed “mild” violations of principles would perhaps lead to a high number of cases with a future ombudsman, more serious violations could lead to a bank being deprived by the Association of Latvian Commercial Banks from advertising its adherence to the Code or from membership in the Association itself. In an increasingly competitive market, banks will consider this outcome as undesirable since a general reputation for unethical practice would obviously hurt business.

SECTION B

DISCLOSURE AND SALES PRACTICES

Good Practice B.1  
**Know Your Customer**

When making a recommendation to a consumer, a bank should gather, file and record sufficient information from the consumer in order to ensure that the bank’s recommendation, product or service is appropriate to that consumer. The extent of information the bank gathers should: (a) be appropriate to the nature and complexity of the product or service being proposed to or sought by the consumer; and (b) enable the bank to provide a professional service.

Description

While some banks have internal rules requiring the application of these practices, these are apparently not yet widespread or routine. There is no reference to these sorts of practices in the Bank’s Code of Conduct and there are no statutory requirements in these respects.

Recommendations

When making a recommendation to a consumer, any Latvian bank should be required, by law, to gather, file and record sufficient information from the consumer in order to ensure that its recommendation, product or service is appropriate to that consumer. The extent of information the bank gathers should: (a) be appropriate to the nature and complexity of the product or service being proposed to, or sought by, the consumer; and (b) enable the bank to provide a professional service.

Good Practice B.2  
**Suitability**

Having regard to the facts disclosed by a consumer and other relevant facts about that consumer of which a bank is aware, the bank needs to ensure that:

- a. Any product or service it offers to that consumer is suitable for that consumer;
- b. In offering a selection of product or service options to that consumer, the product or service options contained in the selection represent only the most suitable from the bank’s range of products or services; and
- c. In recommending a product or service to that consumer, the recommended product or service is, in the reasonable view of the Bank, the most suitable product or service for that consumer.

Description

There is nothing in the existing law or in the Banks’ Code of Conduct that deals explicitly with this topic. As indicated above, by the terms of the Code of Conduct, banks are simply admonished to provide consumers with “comprehensive and honest information on possible risks”. Some banks do voluntarily seek, however, to ensure at least some elements of suitability.

Recommendations

Having regard to the facts disclosed by a consumer and other relevant facts about that consumer of which any bank is aware, the bank needs to ensure that:

- a. any product or service it offers to that consumer is suitable for that consumer;
- b. in offering a selection of product or service options to that consumer, the product or service options contained in the selection represent only the most suitable from the bank’s range of products or services; and
- c. in recommending a product or service to that consumer, the recommended product...
or service is, in the reasonable view of the Bank, the most suitable product or service for that consumer.

In particular, the law must ensure that a credit card is only issued to an identified customer who, after applying for it, has been recognized by its provider as a suitable consumer to receive it.

Suitability rules must be enacted and enforced.

<table>
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<tr>
<th>Good Practice B.3</th>
<th>Credit Agreements with Consumers</th>
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<tbody>
<tr>
<td>Before a consumer enters into a credit agreement with a bank, the bank should:</td>
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<tr>
<td>a. Ensure that its advertising, if any, in respect of such credit cautions the consumer against being an irresponsible borrower;</td>
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<tr>
<td>b. Obtain independently verifiable evidence of the consumer’s assets and liabilities so as to ascertain whether the consumer has the financial capacity to repay the principal of the credit and all interest accruing thereon;</td>
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<tr>
<td>c. Go over each term of the agreement with the consumer and establish to the bank’s reasonable satisfaction that the consumer understands and agrees with each of the terms of the agreement, including the certain, likely and possible future implications of each term;</td>
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<tr>
<td>d. Explain to the consumer the requirements in respect of security to be provided by the consumer for the loan;</td>
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<tr>
<td>e. Explain to the consumer the potential risks that may accrue to him or her in respect of future interest rate adjustments;</td>
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<tr>
<td>f. Explain to the consumer the potential risks that may accrue to him or her in respect of possible future fluctuations in the rate of foreign exchange in the event the credit is denominated other than in local currency;</td>
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<tr>
<td>g. Inform the consumer on the methods of computing interest rates to be paid by or charged to the consumer in accordance with the agreement, any relevant non-interest charges or fees related to the credit offered to the consumer, and any service charges to be paid by the consumer;</td>
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<tr>
<td>h. Ensure that no term or condition of the agreement is misleading or manifestly unfair to the consumer;</td>
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<tr>
<td>i. Disclose to the consumer the bank’s complaints procedures, as well as an outline of the action and remedies which the bank may take in the event of a default by the consumer;</td>
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<tr>
<td>j. Ensure that the agreement is written in plain language and in a font size and spacing that facilitates the reading of every word; and</td>
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<tr>
<td>k. Afford the consumer ample opportunity to read, reflect and comment upon each term of the agreement before the agreement is signed.</td>
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| Description | The Regulation regarding Consumer Credit Agreements\(^ {47}\) prescribes the detailed information that is required to be included in any consumer credit agreement,\(^ {48}\) the exceptions to these basic rules, how annual interest rates are to be calculated and how the total cost of credit. |


\(^{48}\) Ibid. - By Paragraph 2, a “short-term agreement to pay for goods or services by installment” is not considered a ‘credit agreement’.
may be reduced on an equitable basis.

By terms of the Regulation, the annual interest rate is the total cost of the credit (including loan interest and other charges, with certain exceptions stated in the law), expressed as a percentage of the loan granted to the consumer.\(^{49}\) This rate must be calculated in accordance with a formula prescribed under the Regulation. Furthermore, in credit agreements which allow variations in the rate of interest and other charges, which are contained in the annual interest rate but are not specifiable at the time it is calculated, the annual interest rate must be calculated on the assumption that the interest and other charges remain fixed and it is applied until the end of the term of the agreement.\(^{50}\)

It is also noteworthy that if a fixed schedule for repayment of the credit has not been determined and cannot be determined on the basis of the credit agreement's conditions, the credit is repaid in equal monthly instalments during the entire term of the agreement. And, if the expiry date of the agreement has not been specified, it is presumed that the duration of the agreement is one year.\(^{51}\)

For a credit agreement that amounts to an over-draft facility in respect of a consumer's current account, when calculating the annual interest rate, the total credit amount is deemed to have been taken out in its entirety and for the entire term of the credit agreement. If, however, the term of the credit agreement has not been specified, the annual interest rate is calculated, assuming that the credit is repaid within three months.\(^ {52}\)

In advertising the possibility for a consumer to obtain credit, it is indeed forbidden to encourage irresponsible borrowing.\(^ {53}\) Also, any such advertisement must contain information warning the consumer of the need to borrow responsibly and to evaluate his or her ability to repay the credit.\(^ {54}\)

Also, each credit agreement must contain:

1. the annual interest rate and assumptions, if such have been utilised in calculating the annual interest rate;
2. the loan interest rate, as well as the time periods when the interest rate changes and the conditions applicable to such changes;
3. the initial instalment (if such exists), other amounts and payments which the consumer is obliged to pay in order to repay the credit, the number and frequency or definite dates of payments of interest and other costs, as well as the total amount of payments. (if the total amount of payments is not known at the moment of entering into the agreement, the method for calculation thereof must be indicated);
4. a statement of credit cost items (including interest and other charges included in the annual interest rate) and the conditions according to which they may be amended. (If exact amounts are known, those sums must be indicated. If exact amounts are not known, either the method for calculation or as accurate an estimate as possible must be provided);
5. information regarding the right to repay the credit before the end of term and the procedure for the pre-term repayment, as well as the right of the grantor of credit to receive reimbursement for the costs related to early repayment (if such has been provided for in the contract);
6. the required form of guarantee (if such exists);

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\(^{49}\) Ibid, Paragraph 3
\(^{50}\) Ibid, Paragraph 8
\(^{51}\) Ibid, Paragraph 9
\(^{52}\) Ibid, Paragraph 13
\(^{53}\) Ibid, Sub-paragraph 14.1 In determining if an advertisement encourages irresponsible borrowing, the overall content and the way it is presented, its design and the information that is given in the advertisement regarding the credit service, regarding the duty to repay the credit and other information presented that enables the consumer to take an economically based decision, must be taken into consideration;
\(^{54}\) Ibid, Sub-paragraph 14.2
7. the amount of the credit limit (if such exists) or the method to determine that limit;
8. provisions for setting aside the credit agreement; and
9. provisions regarding liability for violations of contractual obligations.  

Any credit agreement in respect of a credit card must indicate the information referred to in 1, 2, 3, 4, 7, 8 and 9 above, as well as the conditions of use of the card and of repayment or the method to determine repayment.  

Any credit agreement by which a grantor of credit has granted a consumer the option to utilise funds exceeding the balance in the consumer’s current account, must, with the exception of a credit card agreement, indicate the information referred to in 1, 2, 4, 7, 8 and 9 above, as well as information regarding payments applied as of entering into the agreement and the conditions by which any change to these payments is permissible.  

Any credit agreement that requires the customer to repay the credit within three months must indicate the information referred to in 2, 3, 5, 6, 7, 8 and 9 above, as well as a statement of credit cost items.  

Any credit agreement for the purchase of immovable property or any credit agreement, the repayment of which is secured by an immovable property mortgage, must indicate the information referred to in 2, 3, 5, 6, 7, 8 and 9 above, as well as information regarding the payment if the credit obligations are fulfilled prior to the determined term (if such can be requested in accordance with Paragraph 30) and the calculation thereof.  

In addition, all amendments and supplements to a credit agreement must be made in writing and signed by both parties.  

Throughout the entire term of the credit agreement, the grantor of credit must inform the consumer regarding any changes in the interest rate of the loan or of changes in respect of any additional relevant payments at least one month before the coming into effect of these changes. Such information must be submitted in writing in the account statement or in any other form, regarding which the grantor of credit and the consumer have agreed. If changes in the loan interest result from changes which have occurred in the floating-interest rate component (RIGIBOR, LIBOR or EURIBOR) and information regarding the floating-interest component of the new loan interest rate is publicly available, including in the premises of the grantor of credit, the Parties to the credit agreement may agree that the information is provided periodically to the consumer.  

The general rule is that a consumer has a duty to pay only those payments indicated in the credit agreement and only for the time period up to the date the consumer has settled his or her credit obligations.  

If the consumer wishes to exercise the right to fulfil of his or her credit obligations before the time period originally provided, the consumer must first inform the grantor of the credit in writing.  

And the grantor of the credit cannot request compensation for the consumer’s fulfilment of his or her credit obligations before the set time period. If the consumer utilizes the right to

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55 Ibid, Paragraph 17
56 Ibid, Paragraph 20
57 Ibid, Paragraph 21
58 Ibid, Paragraph 22
59 Ibid, Paragraph 23
60 Ibid, Paragraph 24
61 Ibid, Paragraph 25
62 Ibid, Paragraph 26
63 Ibid, Paragraph 27
64 Ibid, Paragraph 29
fulfil the credit obligations prior to the determined set period and carries out re-financing with another grantor of credit, only substantiated and reasonable costs may be requested for the costs of administrative expenses assuming such occur.\textsuperscript{65}

Finally, if any information regarding the annual interest rate or other charges has not been provided as required or misleading information has intentionally been supplied in the credit agreement, and that fact has had a decisive influence on the consumer’s decision to enter into the credit agreement, the consumer is obliged only to pay interest set by law.\textsuperscript{66}

In addition, basic provisions in at least certain respects are found in Latvia’s Civil Code. These are as follows:

- A cautious interpretation of contractual language is preferred over others, and on that basis, the interpretation that binds the debtor the least must be preferred;\textsuperscript{67}
- Bilateral transactions which impose duties on both parties shall be interpreted, in case of doubt, against the creditor;\textsuperscript{68} and
- A contract shall be considered to be finally entered into only when the contracting parties have reached complete agreement regarding the essential elements\textsuperscript{69} with the purpose of mutually binding each other.\textsuperscript{70}

With the exception of what is stated below, no statutory obligation exists on a bank to ensure that its consumer has the capacity to repay the principal sum and all interest accruing on any credit.

By the terms of the Consumer Rights Protection Law,\textsuperscript{71} and on an exceptional basis, prior to issuing credit that is at least 100 times the minimum monthly wage,\textsuperscript{72} Latvian banks (and any others engaged in lending to consumers) are obliged:

a) to request and receive a statement from the State Revenue Service regarding the income of the consumer or a statement with similar content from some other State tax administration;\textsuperscript{73} and

b) to document the measures performed so as to evaluate the capacity of the consumer to repay the credit, taking into account the statement referred to under (a) above.

In every instance (i.e. regardless of the amount of the credit), there is, however, a statutory onus in these respects that lies upon the consumer. By Section 73 of the Credit Institutions Law: “upon requesting a credit or entering into a credit relationship with a credit institution ... the client\textsuperscript{74} has the duty to provide, pursuant to the request of the credit institution, complete and accurate information about his or her financial situation and property, including encumbrances on the property ... .”

The Latvian Criminal Code goes further in these respects by providing punishments for fraudulent obtaining and using credit and other loans.

\textsuperscript{65} Ibid, Paragraph 30
\textsuperscript{66} Ibid, Paragraph 31
\textsuperscript{67} Civil Code, Section 1508
\textsuperscript{68} Ibid, Section 1509
\textsuperscript{69} As provided in Section 1470 of the Civil Code
\textsuperscript{70} Ibid, Section 1533
\textsuperscript{71} Section 8 (5) of the Consumer Rights Protection Law
\textsuperscript{72} The credit minimum is thus now LVL 14,000 or about USD 28,000. As of 9 June 2009, the minimum monthly wage prevailing from 1 January 2009 was decreased from LVL 180 to LVL 140 (or approximately USD 280 at the rate of exchange as of the same date). Following Bulgaria and Romania, Latvia has the third lowest minimum wage in Europe.
\textsuperscript{73} No such statement can, however, be requested if the consumer is a State official and information regarding his or her income is publicly accessible.
\textsuperscript{74} The term “client” is defined broadly in Section 1 of the Credit Institutions Law as being “a person to whom a credit institution provides financial services.”
Anyone who knowingly provides false information to a creditor whether to obtain a loan or during the term of the loan, is subject to imprisonment for not more than two years or community service, or a fine not exceeding fifty times the minimum monthly wage, with or without deprivation of the right to engage in entrepreneurial activity for a term of not less than two years and not exceeding five years.75

Also, any consumer who uses the proceeds of a loan other than for the purposes provided for in the loan agreement is subject to imprisonment for not more than four years, or community service, or a fine not exceeding sixty times the minimum monthly wage, with or without deprivation of the right to engage in entrepreneurial activity for a term of not less than two years and not exceeding five years.76

Latvia’s Consumer Rights Protection Law provides for the concept of “unfair contractual terms”, the Unfair Commercial Practices Prohibition Law does the same regarding “unfair commercial practices” and these laws make these terms and practices illegal.

The concept of unfair contractual terms is based on the statutory requirement of legal equality in contracts between consumers and Latvian financial institutions.77

By law, contracts do not meet the required test of “legal equality” if they:

- reduce the liability of a party as prescribed by law;
- restrict the consumer’s right to enter into contracts with third parties;
- stipulate privileges to the service provider, and restrictions to the consumer;
- stipulate that the consumer is waiving his or her lawful rights; or
- place the consumer in a disadvantageous position and are contrary to the requirements of good faith.78

Also by law, any contractual term is deemed “unfair”, and thus illegal, if it:

a) has not been mutually discussed by the contracting parties and operates to the disadvantage of the consumer and contrary to the requirements of good faith;

b) does not meet the test of legal equality as indicated above;

c) restricts or excludes the possibility of the consumer exercising the lawful right to claim if the service provider has failed to perform contractual obligations, or has performed them only partially;

d) imposes a disproportionately large contractual penalty upon a consumer in the event the consumer’s contractual obligations are not performed;

e) provides for a determination of the price of services at the moment of supply, or permits the service provider to increase the price without giving the consumer the right to revoke the contract if the final price is unreasonably high compared to the price the contracting parties initially agreed;

f) restricts the duty of the service provider to perform obligations undertaken by its representative, or subjects such obligations to formalities;

g) excludes or hinders the consumer’s right to apply to consumer rights protection institutions or to the court, and provides for adjudication of disputes only in arbitration court;

h) permits a service provider to withdraw unilaterally from a contract unless such a possibility is ensured also for the consumer, or permits a service provider to

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75 Criminal Code, Section 210 (1)
76 Ibid, Section 210 (2)
77 See Section 6 (1) of the Consumer Rights Protection Law
78 See Section 5 of the Consumer Rights Protection Law
terminate a contract unlimited in time without warning;

i) provides for an automatic extension of the term of a contract if the consumer does not give notice seeking the non-extension of the contract, and fixes an unjustifiably short time for the consumer to provide such notice;

j) permits a service provider to retain the amount paid by a consumer if the consumer withdraws from the contract, but does not provide the possibility for a consumer to receive an equivalent amount if the service provider withdraws from the contract;

k) permits a service provider, without the consent of the consumer, to transfer its rights and duties, thereby reducing the amount of guarantees to the consumer; or

l) permits a service provider to unilaterally amend the provisions of a contract or the characteristics of the services.79

In addition, contractual terms must be expressed in plain and comprehensible language, with any ambiguous or imprecise terms in a written contract being interpreted in favor of the consumer.80

In addition, it is provided by law that a commercial practice is unfair,81 if it:

1) does not conform with professional diligence and negatively affects or may negatively affect the economic behavior of such average consumer or such average consumer group to which such commercial practice is addressed or to whom it concerns; or

2) is misleading; or

3) is aggressive.

And, as is true of unfair contractual terms, any unfair commercial practice is prohibited.82

A commercial practice does not conform to professional diligence, if it is performed with less proficiency and diligence than a consumer may justifiably expect in the relevant field of economic or professional activity.83

Furthermore, a commercial practice is deemed to have a negative influence on a consumer’s economic activity, if it substantially limits the possibility of a consumer taking a decision to enter into a contract on the basis of full information.84 What constitutes a “substantial” limitation depends on the facts and is inevitably subject to interpretation.

In addition, a commercial practice is deemed misleading if, taking into account all the circumstances, the consumer, under the influence thereof, takes or may take a decision regarding the entering into a contract, which he or she would otherwise not have taken. A commercial practice is regarded as misleading if:

- misleading information is provided within the framework thereof or such information misleads or may mislead the average consumer, even if it is factually correct;

- the performer thereof unfairly utilizes measures to promote the performer’s services, including comparative advertising that causes confusion regarding the
service or the provider of the service; or
• the performer thereof does not observe the obligations provided for in the good practice code, even though he or she has undertaken to fulfill them and has indicated that he or she is bound by the good practice code.\textsuperscript{85}

Furthermore, a commercial practice is deemed to be \textbf{misleading} if, taking into account its features and circumstances, as well as the limitations of the communication medium:

1) \textbf{significant information} is omitted, which is necessary for an average consumer in order to take a decision; or

2) the performer thereof hides \textbf{significant information} or provides it in an unclear, unintelligible, ambiguous or untimely manner with the result that an average consumer decides or may decide to enter into a contract, which he or she would not have done otherwise.\textsuperscript{86}

Once again, what constitutes “significant” in these respects depends on the facts and is subject to interpretation.

In the event the performer of a commercial practice invites a consumer to purchase a product or receive a service and specifies the features and price of the product or service, \textbf{the following information is deemed by law to be significant}:

1) the main characteristics of the product or service, to the extent possible for the specific product or service, taking into account the communication medium utilized;

2) the address and identity of the performer of the commercial practice and, if such performer acts on behalf of another performer, the address and identity of this other performer;

3) the price (inclusive of taxes) or (where the nature of the product or service means that the price cannot reasonably be calculated in advance) the manner in which the price is calculated, as well as all additional charges, if any, or, (where these charges cannot reasonably be calculated in advance) the fact that such additional charges may be charged by the performer of commercial practices;

4) the arrangements for payment, delivery, performance of the contract and the complaint handling policy, if they depart from the requirements of professional diligence; and

5) the right of refusal.\textsuperscript{87}

In addition, information required to be provided in accordance with other regulatory enactments dealing with the consumer rights’ protection or the provision of services, including information regarding distance contracts, distance financial service contracts, consumer credit contracts, the prices of services, private pension funds and insurance contracts is regarded by law as “\textbf{significant}.”\textsuperscript{88}

Furthermore, the Law sets out circumstances where a \textbf{commercial practice is also deemed misleading} due to actions of the performer of the practice:

A commercial practice is deemed “\textbf{aggressive}” if, after taking into account all of its features and circumstances, it may be concluded that by harassment, coercion, including the use of physical force, or \textbf{undue influence}, it significantly impairs or is likely to significantly impair the average consumer’s freedom of choice or conduct with regard to the product, with the

\textsuperscript{85} Ibid, Section 9 (1)
\textsuperscript{86} Ibid, Section 10 (1)
\textsuperscript{87} Ibid, Section 10 (3)
\textsuperscript{88} Ibid, Section 10 (4)
result that the consumer takes or may take a decision regarding the entering into a contract, which he or she would not have taken otherwise. The Law states the elements that need to be assessed in order to determine whether undue influence has been exercised in a commercial practice.

Furthermore, the Law states the types of individual actions that can cause a commercial practice to be regarded as aggressive.

The question immediately arises how statutory understanding, interpretation, application and enforcement of all of the above can possibly be carried out effectively and professionally within the CRPC, an institution that is without any senior staff having legal training. It would inevitably be a difficult task for highly trained judges having expertise in financial sector issues to interpret and enforce these and all of the related provisions.

**Recommendations**

While many important aspects of good practices in these respects are "state-of-the-art", before a consumer enters into a consumer credit agreement with a bank, consideration should be given to requiring banks to:

a. seek and obtain independently verifiable evidence of the consumer’s assets and liabilities so as to ascertain whether the consumer has the financial capacity to repay the principal of the credit and all interest accruing thereon (banks usually follow this procedure, although they are not required to do so);

b. explain to the consumer the potential risks that may accrue to him or her in respect of future interest rate adjustments;

c. explain to the consumer the potential risks that may accrue to him or her in respect of possible future fluctuations in the rate of foreign exchange in the event the credit is denominated other than in local currency;

d. disclose to the consumer the bank’s complaints procedures, as well as an outline of the action and remedies which the bank may take in the event of a default by the consumer;

e. ensure that the agreement is written in plain language and in a font size and spacing that facilitates the reading of every word; and

f. afford the consumer ample opportunity to read, reflect and comment upon each term of the agreement before the agreement is signed.

**Good Practice B.4 Cooling-off Period**

Unless explicitly waived in advance by a consumer in writing, a bank should provide the consumer a “cooling-off” period of at least seven, but preferably fourteen, days immediately following the signing of any loan agreement between the bank and the consumer during which time the consumer may, on written notice to the bank and the return of all monies received, treat the agreement as null and void without penalty to the consumer of any kind.

**Description**

The basic rules of contract in these respects are contained in Latvia’s Civil Code which, among other things, provides as follows:

- A contract that has been legally entered into imposes on a contracting party a duty to perform what has been promised, and neither the exceptional difficulty of the transaction, nor difficulties in performance arising later, gives the right to one party to withdraw from the contract, even if the other party is compensated for losses.

--89 Ibid, Section 12 (1)
--90 Ibid, Section 12 (3)
--91 Ibid, Section 13
--92 Civil Code, Section 1587
• One party may not withdraw from a contract without the consent of the other party, even if the other party fails to perform and the effort to withdraw is due to that failure;93
• Unilateral withdrawal from a contract is permitted only when it is based on the nature of the contract, or when the law provides for it in certain circumstances, or when such right has been expressly provided for by contract;94 and
• Each party has the right to claim for performance of the contract by the other party.95

As permitted by Section 1589 of the Civil Code, withdrawal is allowed by statute under the Consumer Rights Protection Law. By Section 12 of this Law, the consumer has the right “to withdraw unilaterally from a contract within a specified time period without payment of penalties, interest or compensation for losses.”96 But this right can only be exercised if:

a) the contract was entered into outside the “permanent location of provision of services”; or
b) a so-called “distance contract” was in question; or
c) the contract involved obtaining the right of temporary occupancy of the whole or part of a residential building.

In these three instances, at the time the contract takes effect, the service provider is obliged to submit to the consumer a written withdrawal form indicating the name and address of the provider, as well as a description of the right of withdrawal. In the case of a bank, by sending the withdrawal within a specified time period, the contract is terminated and the consumer released from any contractual obligations. While it is the duty of the consumer to return “goods” within seven days following the date the consumer sends the completed written withdrawal form, the Consumer Rights Protection Law does not provide any “specified time” to return funds received from a service provider.97

Furthermore, by Section 31 of the Consumer Rights Protection Law, a consumer is entitled to withdraw unilaterally from a consumer credit contract “if he or she exercises the right of withdrawal provided in Section 12 of this Law”.

As far as “distance contracts” are concerned, applicable Regulations entitle a consumer to withdraw unilaterally within a period of 14 days.98 However, unless the contracting parties have agreed otherwise, a consumer may not use the right of withdrawal regarding any contract where the execution of which has been fully completed at the explicit request of the consumer and before he or she exercises the right of withdrawal.99 Furthermore, in the event the consumer exercises the right of withdrawal, the service provider may require the consumer to pay without “undue delay” for the services actually provided in accordance with the distance contract. This is for the simple reason that performance of a distance contract may only begin after a consumer has given his or her consent.100 In such a case, the amount to be paid: (a) cannot exceed “the amount which is in proportion to the extent of the service already provided” when measured against the full extent of the service provider’s commitments; and (b) “is not an amount which can be regarded as a penalty”.101

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93 Ibid, Section 1588
94 Ibid, Section 1589
95 Ibid, Section 1590
96 See Section 12 (1)
97 See subsections (2) through (5) of Section 12
98 See Paragraph 19 of the Regulations regarding Distance Contracts for the Provision of Financial Services (Cabinet Regulation No. 1037 of 21 December 2004). In addition, by the same paragraph, a consumer may unilaterally withdraw from a distance contract relating to life insurance and private pension transactions within a period of 30 days.
99 Ibid, paragraph 21 (3)
100 Ibid, paragraph 25
101 Ibid, paragraphs 25.1 and 25.2
There is no guidance, however, as to what constitutes “undue delay” or “penalty”.

Before a distance contract can be entered into, a service provider must provide the consumer with: information regarding his or her right of withdrawal; the time period in which such right can be exercised; information regarding the amount the consumer may be required to pay if withdrawal occurs; as well as the consequences of non-exercise of the right of withdrawal.\(^\text{102}\)

Although there is nothing in the Code of Conduct of the Association of Latvian Commercial Banks on this matter, in at least some banks the practice has been to allow consumers to treat credit contracts as terminated provided the consumer first returns all funds borrowed and pays an “administrative” fee for doing so. There are apparently, however, no consistent or transparent rules regarding the application of such fees or the basis on which they are calculated, whether in generally applicable terms and conditions of banks or in the specific wording of individual consumer loan agreements.

### Recommendation

Consideration should be given to amending the law to apply the distance contract provisions to all loans to consumers (i.e. unless explicitly waived in advance by a consumer in writing, a bank must provide the consumer a “cooling-off” period of 14 days immediately following the signing of any loan agreement between the bank and the consumer during which time the consumer may, on written notice to the bank and the return of all monies received, treat the agreement as null and void without penalty to the consumer of any kind).

### Good Practice B.5

**Linked Products and Bundling Clauses**

Whenever a borrower is obliged by a bank to purchase any product, including an insurance policy, as a pre-condition for receiving a loan from the bank, the borrower should be free to choose the provider of the product.

### Description

There is nothing in the Latvian law or in the Code of Conduct of the Association of Latvian Commercial Banks that deals explicitly with this matter.

While banks properly set their own insurance requirements for borrowers in order to allow a loan transaction, the present practice is marred by banks:

- setting their own requirements as to insurance company qualifications and insurance cover needed in respect of certain lending operations;
- providing borrowers with a list of approved insurance companies that meet the banks’ “stringent” requirements in these respects;
- ensuring that any insurance company that is affiliated with the bank (i.e. has direct or indirect common ownership) is on the bank’s list; and
- not informing their borrowers of these facts.

Another common practice is the bundling of payment accounts with mortgages, which is provided for under existing regulations. A problem with this practice is that if the terms of the payment account change during the course of the mortgage contract with the imposition of fees, consumers are unable to switch to another provider without incurring disproportionate charges.

### Recommendations

Bundling of products should only be permissible by law if the consumer: (1) receives prior transparent notice in writing of the bundling and clear statements regarding: (a) its implications in terms of cost to the consumer; and (b) the nature of the bundling and what precisely is and is not covered; and (2) then agrees in writing to waive his or her right to proceed with unbundled products.

Consideration should be given to amending the law so as to require full disclosure in the event that any accompanying services are offered in the context of a consumer loan.

\(^{102}\) Ibid, paragraph 8.1
### Good Practice B.6 

**Preservation of Rights**

Except where permitted by applicable legislation, in any communication or agreement with a consumer, a bank should not exclude or restrict, or seek to exclude or restrict:

- a. Any statutory liability or duty of care of the bank to the consumer;
- b. Any duty to act with skill, care and diligence toward the consumer in connection with the provision by the bank of any financial service or product; or
- c. Any liability arising from the bank's failure to exercise the degree of skill, care and diligence that may reasonably be expected of it in the provision of any financial service or product to the consumer.

### Description

It appears that, at least in general terms, in their communications and agreements with consumers, Latvian banks adopt this good practice.

Although the term “duty of care” is not employed in Latvian legislation, the extensive statutory obligations of a bank to a consumer as provided in the Consumer Rights Protection Law and the Unfair Commercial Practices Prohibition Law are tantamount to the same concept.

In particular, it is important to note that, as of June 23, 2009, service providers (i.e. banks in this case) must exercise professional diligence and act honestly with their consumers.  

Also, the Civil Code provides as follows:

- A person who allows a delict (i.e. a wrongful act per se, as a result of which harm has been caused) to take place is liable for it if, as an employer, the person has the opportunity, and therefore the duty, to prevent such wrongful act;  
- A person who fails to exercise due care in choosing employees and to be satisfied as to their abilities and suitability to perform the duties imposed on them, is liable for losses an employee thereby causes to a third person;  
- A person who has instructed another person to perform a wrongful act is liable for the action of the other person, notwithstanding that the act of such person exceeds the limits of the instructions. A person who has given another person cause for such action as results in losses to a third person, is similarly liable;  
- The lender is liable to the borrower for all losses inflicted through acts in bad faith, such as reclaiming the property before due time, but is not liable for mere negligence;  
- If a person is at fault for inflicting harm upon another without wrongful intent, such person acted negligently. Negligence can be gross or ordinary;  
- A person acts with gross negligence if the person's conduct is reckless and careless in the highest degree; or if the person acts with less care towards the property of another than the person would apply to his or her own property; or if the person initiates a course of action, the harmfulness of which could and should have been known to him or her. In terms of compensation for losses and other legal consequences, gross negligence is equivalent to wrongful intent;

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103 See Section 21.2 of the Consumer Rights Protection Law in force as of 23 June 2009.
104 Civil Code, Section 1639
105 Ibid, Section 1782
106 Ibid, Section 1781
107 Ibid, Section 1966. This appears to conflict with the provisions of the Consumer Rights Protection Law as well as the Unfair Commercial Practices Prohibition Law.
108 Ibid, Section 1644
109 Ibid, Section 1645
Ordinary negligence is that lack of care and due diligence as must be observed by any reasonably prudent and careful manager;\(^{110}\)

When a person gives the same kind of care to the property of another as the person usually does to his or her own property, the person is not liable for negligence unless such negligence was gross;\(^{111}\)

Every wrongful act per se, as a result of which harm has been caused, gives the person who has suffered the harm the right to claim satisfaction from the infringer, insofar as the infringer may be held at fault for such act;\(^{112}\) and

Everyone has a duty to compensate for losses they have caused through their acts or failure to act.\(^{113}\)

What is more, there are draconian criminal law implications if a person (i.e. a bank officer) fails to ensure the quality of services. If a paid service is knowingly provided by a person to a consumer while failing to comply with requirements set out in regulatory enactments, technical standards documents or any agreement, with the result that substantial harm is caused to the health or property of the consumer, that person is liable to imprisonment not exceeding five years, or custodial arrest, or community service, or a fine not exceeding sixty times the minimum monthly wage, with or without deprivation of the right to engage in specific forms of entrepreneurial activity for a term of not less than two years and not exceeding five years.\(^{114}\)

Like all criminal law provisions, this provision cannot be mitigated or excluded by agreement or otherwise. The degree of harm that meets the test of “substantial” is, however, left to the courts.

**Recommendations**

Personal liability for the failure of an officer of a financial institution in his or her dealings with a retail consumer should be transferred from the Criminal Code to civil legislation so that personal liability can be enforced more easily than currently.

**Good Practice B.7  Regulatory Status Disclosure**

In all of its advertising, whether by print, television, radio or otherwise, a bank should disclose: (a) that it is regulated; and (b) the name and address of the regulator.

**Description**

The Credit Institutions Law simply allows the words “credit institution” or “bank” or a combination thereof to be used in the name of a company that is licensed to operate as such. However there is no mention of any requirement to disclose that the company is regulated and by whom.\(^{115}\)

Likewise, there is no requirement in the Advertising Law for a bank to disclose this information.

Nor is there any provision in this respect in the Banks’ Code of Conduct.

The latest amendments to the Consumer Rights Protection Law require a service provider (i.e. a bank) to “inform the public of its full corporate name and working hours,”\(^{116}\) but this obviously does not address the additional specific requirement referred to above.

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\(^{110}\) Ibid, Section 1646

\(^{111}\) Ibid, Section 1647

\(^{112}\) Ibid, Section 1635, paragraph 1

\(^{113}\) Ibid, Section 1779

\(^{114}\) Criminal Code, Section 202

\(^{115}\) See Section 9 (1) of the Credit Institutions Law

\(^{116}\) Section 21.3 of the Consumer Rights Protection Law, in force as of 23 June 2009
### Recommendation

The law should be amended to require any Latvian bank to disclose in any advertising: (a) that it is regulated by the Finance and Capital Market Commission; and (b) the name and address of the FCMC. Or, at the very least, this requirement should be included in any new or revised industry Code of Conduct.

### Good Practice B.8

**Terms and Conditions**

Before a consumer may open a deposit, current or loan account at a bank, the bank must provide the consumer with a written copy of its general terms and conditions, as well as all terms and conditions that apply to the account to be opened. Collectively, these Terms and Conditions must:

- a. Disclose details of the bank’s general charges, the bank’s complaints procedures, information about any compensation scheme that the bank is a member of, and an outline of the action and remedies which the bank may take in the event of a default by the consumer;
- b. Include information on the methods of computing interest rates paid by or charged to the consumer, any relevant non-interest charges or fees related to the product offered to the consumer, any service charges to be paid by the consumer, restrictions, if any, on account transfers by the consumer and the procedures for closing an account;
- c. Set forth clear rules regarding: (i) the reporting of unauthorized transactions; (ii) stolen cards; and (iii) liability; and
- d. Be written in plain language and in a font size and spacing that facilitates the reading of every word.

### Description

Although a bank does not have any obligation at any time to provide a consumer a written copy of its general terms and conditions, before a consumer may make a deposit in any bank (or credit union), the bank (or credit union) is obliged, by law, to provide information to the consumer regarding the guaranteed compensation amount and its payment procedures in accordance with the Deposit Guarantee Law.\(^\text{117}\)

As far as the Bank’s Code of Conduct is concerned:

- a) “at the time of opening an account in the customer’s name, banks will provide the client with all required information on performance of banking services [and] at the request of a customer, banks will also provide customers with relevant additional information”\(^\text{118}\)
- b) “banks service provisions will be expressed in clear wording in writing and will be an honest and well-balanced account of the relations between a customer and a bank”;\(^\text{119}\)
- c) “a bank will provide new customers with a written summary or explanation of the essential features of offered services”;\(^\text{120}\) and
- d) “comprehensive written information regarding appeal processing procedures will be freely available at the bank and on the bank’s website”.\(^\text{121}\)

Under (a) above, it is for a bank to resolve itself, not only what is “required information”, but also what constitutes “relevant additional information” in the event the customer views what the bank considers “required information” as inadequate. Under (c) above, it is also for a bank to decide itself what features of offered services are “essential”. This vagueness and subjectivity works to the disadvantage of all concerned.

There is nothing in the Bank’s Code of Conduct suggesting that banks should have general conditions of consumer lending that are clear to the borrower and establish accurate rules in

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\(^\text{117}\) Deposit Guarantee Law, Article 20 (1)  
\(^\text{118}\) Principle VII  
\(^\text{119}\) Principle XII (1)  
\(^\text{120}\) Principle XII (2)  
\(^\text{121}\) Principle XIII (2)
respect of the loan account and debt repayment.

However, the regime for contractual terms and commercial practices that are unfair to the consumer is provided in detail in the Consumer Rights Protection Law and the Unfair Commercial Practices Prohibition Law.

Finally, regarding item d. of the good practice, the only statutory requirement to employ “plain and comprehensible language” comes in Section 6 (2) of the Consumer Rights Protection Law, but this is in respect of contractual terms only.\textsuperscript{122}

The Regulations\textsuperscript{123} regarding Consumer Credit Agreements set out in some detail what must form part of the credit agreement. However there is no requirement for any pre-contractual information relating to consumer credit or mortgage credit.

The Regulations set out the methods for calculating interest rates, and establishes that the lender has a duty to inform the borrower in writing if there are any changes in interest rates. The Regulations further stipulate that the APR should be disclosed clearly in any advertising and that any advertising should carry a warning about the need to borrow responsibly. However it is not clear how these regulations are enforced or who has the power to enforce them.

Further, the regulations set out the duties of the consumer in terms of repaying the debt including what should happen in the case of any early repayment. The borrower has a unilateral right to the early repayment of credit in Latvia. The lender does not have the right to ask for compensation. They are only allowed to assume that the payment is made on the next scheduled payment date and include any interest accrued. Relative to other jurisdictions in Europe, this is a very pro-consumer rule. The downside of such regulations is that it means that fixed rate mortgages are unlikely to be offered with long fixed rate periods, as the banks will be unwilling to take on the interest rate risk. Long term fixed rates can offer greater security and certainty to consumers.

There are no requirements to provide any advice or guidance to the consumer with regards to the potential risks associated with the financial products arising from either interest rate movements or currency movements.

**Recommendation**

Consideration should be given to requiring by statute that, before a consumer opens a deposit, current or loan account at any bank, the bank must provide the consumer with a written copy of its general terms and conditions, as well as all terms and conditions that apply to the account to be opened. These Terms and Conditions should then:

i) disclose details of the bank’s general charges, the bank’s complaints procedures, information about any compensation scheme that the bank is a member of, and an outline of the action and remedies which the bank may take in the event of a default by the consumer;

ii) include information on the methods of computing interest rates paid by or charged to the consumer, any relevant non-interest charges or fees related to the product offered to the consumer, any service charges to be paid by the consumer, restrictions, if any, on account transfers by the consumer and the procedures for closing an account;

iii) set forth clear rules regarding: (a) the reporting of unauthorized transactions; (b) stolen credit and debit cards; and (c) liability; and

iv) be written in plain language and in a font size and spacing that facilitates the reading of every word.

\textsuperscript{122} By this same sub-section, “ambiguous and imprecise terms of a written contract shall be interpreted in favor of the consumer”.

\textsuperscript{123} Cabinet Regulation 692, adopted 25 August 2008, Regulations concerning Consumer Credit Agreements.
In this respect, the provisions of the EU Directive 2008/48/EC of 23 April 2008 are relevant. A further practice which is becoming common in many European countries is to provide the consumer with some stress tests of the products they are purchasing. This is largely applicable to mortgage loans which may be subject to wide variations in cost due to variable interest rates or currency movements.

The Association of Latvian Commercial Banks should produce a standard set of easily understandable scenarios which should then be given to consumers — prior to signing a credit agreement. The scenarios could include the impact of increasing the interest rate by 2 or 3 per cent, or the impact of a change in the value of the LVL in relation to the currency of the mortgage loan. This information could form part of the Key Facts document detailed below.

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<tr>
<th>Good Practice B.9</th>
<th><strong>Key Facts Document</strong></th>
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<tr>
<td>a.</td>
<td>A bank should have a single-page Key Facts Document, written in plain language, in respect of each of its accounts, types of loans or other products.</td>
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<tr>
<td>b.</td>
<td>Prior to a consumer opening any account at, or signing any loan agreement with, the bank, the consumer should have delivered a signed statement to the bank to the effect that he or she has duly received a copy of the relevant document from the bank.</td>
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</table>

**Description**

Neither the law requires a bank to produce such document, nor the Bank’s Code of Conduct recommends this practice. That said, the kernel of the idea is contained in various provisions of the Banks’ Code of Conduct. By Article VII (1), “[i]nformation on essential bank services, regulations and prices shall be freely available at customer service sites” and by Article VII (3), banks are to counsel their customers “on the regulations of provided services, including the provision of comprehensive and honest information on possible risks.” However, no bank appears to use Key Facts Documents for any of their accounts or loan products.

Regarding mortgages, two banks[^124] have signed the European Agreement on a Voluntary Code of Conduct on Pre-Contractual Information for Home Loans, although implementation is not scheduled until later this year for one and 2010 for the other. The Code of Conduct includes the European Standardised Information Sheet (ESIS), which is a format that provides consumers with standardized key product information[^125]. It would be relatively straightforward to implement the Code of Conduct across the banking sector, given that all Nordic banks already implement the Code in their own countries, where it forms part of the standard pre-contractual information pack for home loans.

**Recommendations**

The law should be amended to require banks to provide a Key Facts Document for each product or service being offered to any of its customers. And, prior to a consumer opening any account at, or signing any loan agreement with, a bank, the consumer should have delivered a signed statement to the bank to the effect that he or she has duly received a copy of the relevant Key Facts Document from the bank.

The Association of Latvian Commercial Banks should fully implement the European Code of Conduct on Home Loans. This could either be done on a voluntary basis or by regulation, if necessary.

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<th>Good Practice B.10</th>
<th><strong>Guarantees</strong></th>
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</thead>
<tbody>
<tr>
<td>No advertisement by a bank should describe either an actual or future deposit or interest rate payable on a deposit as being guaranteed or partially guaranteed unless:</td>
<td></td>
</tr>
</tbody>
</table>

[^124]: JSC Rietumu Banka and SEB Bank

<table>
<thead>
<tr>
<th>Description</th>
<th>By the terms of the Civil Code:</th>
</tr>
</thead>
<tbody>
<tr>
<td>• A contract promising that a third person will perform something binds neither the promisor nor the third person, unless:</td>
<td></td>
</tr>
<tr>
<td>i) someone undertakes the obligations of another person's debt;</td>
<td></td>
</tr>
<tr>
<td>ii) someone promises to procure a guarantor for oneself;</td>
<td></td>
</tr>
<tr>
<td>iii) a person's manager makes a promise and asserts that this third person shall confirm it; or</td>
<td></td>
</tr>
<tr>
<td>iv) a promise has been made securing performance with contractual penalties or by undertaking to compensate for any loss.</td>
<td></td>
</tr>
<tr>
<td>In all such cases, contractual penalties or compensation for losses shall be paid if the promise is not kept;(^{126}) and</td>
<td></td>
</tr>
<tr>
<td>• If someone makes a promise either to ensure that a third person performs something, or to induce him or her to perform it, then it shall be an action of the promisor himself or herself, and therefore, the promisor shall compensate for losses if the third person does not undertake to perform such action.(^{127})</td>
<td></td>
</tr>
</tbody>
</table>

Regardless of any underlying substantive law, however, besides the existing deposit insurance regime (which is based upon legally enforceable statutory obligations),\(^{128}\) there is nothing in the Advertising Law, the Credit Institutions Law, the Civil Code, or apparently any other Code, Law or regulation that deals in any way with advertisements of guarantees of a bank deposit or of guarantees of an interest rate payable on a bank deposit. And there is, likewise, nothing in the Banks’ Code of Conduct that touches on this subject.

<table>
<thead>
<tr>
<th>Recommendation</th>
<th>The law should require that no advertisement by a Latvian bank may be made that describes either an actual or future deposit or interest rate payable on a deposit as being guaranteed or partially guaranteed unless:</th>
</tr>
</thead>
<tbody>
<tr>
<td>a.</td>
<td>there is a legally enforceable agreement between the bank and a third party who or which has provided the guarantee; and</td>
</tr>
<tr>
<td>b.</td>
<td>the advertisement states:</td>
</tr>
<tr>
<td></td>
<td>(i) the extent of the guarantee;</td>
</tr>
<tr>
<td></td>
<td>(ii) the name and address of the party providing the guarantee; and</td>
</tr>
<tr>
<td></td>
<td>(iii) in the event that that party is in any way connected to the bank, the precise nature of that connection.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Good Practice B.11</th>
<th>Professional Competence</th>
</tr>
</thead>
<tbody>
<tr>
<td>a.</td>
<td>In order to avoid any misrepresentation of fact to a consumer, any bank staff member who deals directly with consumers, or who prepares bank advertisements or who markets any service or product of the bank should be familiar with all legislative, regulatory and code of conduct guidance requirements relevant to his or her work, as well as with the details of any product or service of the bank which he or she sells or promotes.</td>
</tr>
<tr>
<td>b.</td>
<td>Regulators and industry associations should collaborate to establish and administer minimum competency requirements for any bank staff member</td>
</tr>
</tbody>
</table>

\(^{126}\) Civil Code, Section 1546  
\(^{127}\) Ibid, Section 1547  
\(^{128}\) See Good Practice F. 1 below.
who:
(i) deals directly with consumers;
(ii) prepares any Key Fact Document or any advertisement for the bank;
or
(iii) markets the bank’s services and products

| Description | Some banks, and apparently all that are foreign-owned, take it upon themselves to ensure that their staff members (at least those under categories b (i) and (iii) above) receive what they consider to be “adequate” in-house training before staff embark on client-oriented functions. But from the perspective of what would be best for the banking industry and for consumers, unfortunately no generally agreed industry standard in these respects exists yet in Latvia.

The Banks’ Code of Conduct suggests that banks should “carefully choose and supervise their personnel, as well as regularly upgrade its qualification, in order to ensure high quality and fair provision of banking services.” No objective standards are yet forthcoming, however, as to what constitutes “high quality” and how this should be objectively tested and enforced.

While the Association of Latvian Commercial Banks provides an 18-month certificate course in specialized training for senior bankers seeking to improve their professional qualifications, these courses are not meant for bank tellers and loan officers who deal on a daily basis with consumers.

Viewed from the perspective of what is not permissible, however, it is relevant to note that Latvia’s Criminal Code penalizes those who exceed their authority, use authority in bad faith or are neglectful. The relevant Criminal Code provisions are as follows:

- If a responsible employee of a company (e.g. a bank), (i.e. a person who has the right to make decisions binding on other persons or the right to deal with the property or financial resources of the company, or a person similarly authorized by the company), carries out an intentional act in bad faith using his or her authority or exceeding such, and such an act causes “substantial harm” to ... rights and interests protected by law of another person, that person is liable on conviction to imprisonment for up to three years, or custodial arrest, or community service, or a fine not exceeding eighty times the minimum monthly wage;

- If a person neglectfully fulfills his or her employment duties, whether as a responsible employee of a company (e.g. a bank) or a person similarly authorized by a company, and “substantial harm” is caused thereby to the .... rights and interests protected by law of another person, that person is liable on conviction to imprisonment for up to two years, or custodial arrest, or community service, or a fine not exceeding forty times the minimum monthly wage.

| Recommendation | The Association of Latvian Commercial Banks, possibly with the collaboration of the CRPC, should establish and administer minimum competency requirements at the very least for any staff member of a bank who:

- deals directly with consumers;
- prepares any Key Fact Document or any advertisement for the bank; or
- markets the bank’s services and products.

SECTION C  
CUSTOMER ACCOUNT HANDLING AND MAINTENANCE

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129 Principle IV (1)
130 See Section 196 (1) of the Criminal Code
131 Ibid, Section 197
### Good Practice C.1 — Statements

<table>
<thead>
<tr>
<th>Statements</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. Unless a bank receives a customer’s prior signed authorization to the contrary, the bank should issue, and provide the customer with, a monthly statement regarding every account the bank operates for the customer. Each such statement should:</td>
</tr>
<tr>
<td>(i) set out all transactions concerning the account during the period covered by the statement; and</td>
</tr>
<tr>
<td>(ii) provide details of the interest rate(s) applied to the account during the period covered by the statement.</td>
</tr>
<tr>
<td>b. Each credit card statement must set out the minimum payment required and the total interest cost that will accrue, if the cardholder makes only the required minimum payment.</td>
</tr>
<tr>
<td>c. Each mortgage or other loan account statement must clearly indicate the amount paid during the period covered by the statement, the total outstanding amount still owing, the allocation of payment to the principal and interest and, if applicable, the up-to-date accrual of taxes paid.</td>
</tr>
<tr>
<td>d. A bank must notify a customer of inactivity of any account of the customer and provide a reasonable final notice in writing to the customer if the funds are to be transferred to the government.</td>
</tr>
<tr>
<td>e. When an investor signs up for paperless statements, such statements should be in an easy-to-read and readily understandable format.</td>
</tr>
</tbody>
</table>

### Description
Not all of these provisions are covered by existing regulations.

### Recommendation
The regulations need to be expanded to cover all aspects referred to above and then effectively enforced.

### Good Practice C.2 — Notification of Changes in Interest Rates and Non-interest Charges

<table>
<thead>
<tr>
<th>Notification of Changes in Interest Rates and Non-interest Charges</th>
</tr>
</thead>
<tbody>
<tr>
<td>A customer of a bank must be notified in writing by the bank of any change in:</td>
</tr>
<tr>
<td>a. The interest rate to be paid or charged on any account of the customer, as soon as practicably possible; and</td>
</tr>
<tr>
<td>b. A non-interest charge on any account of the customer, a reasonable period in advance of the effective date of the change.</td>
</tr>
</tbody>
</table>

### Description
In accordance with the Regulations regarding Consumer Credit Agreements, throughout the term of a bank’s credit agreement with a consumer, the bank is obliged to inform the consumer of any changes in the interest rate of the loan or of any other relevant payments one month before the coming into effect of these changes. Such information must be submitted in writing (either in the account statement or otherwise), as the bank and consumer have agreed. If a change in interest results from a change in the floating-interest rate (RIGIBOR, LIBOR or EURIBOR) and information regarding the floating interest rate component is publicly available, including in the bank’s premises, the bank and consumer may agree that this information can be provided periodically to the consumer.

The ultimate protection to any consumer comes from the Criminal Code which provides for punishment for usury as follows: a person (including a bank) who makes a loan, knowingly taking advantage of the grave economic situation of the borrower, and setting up terms and conditions which are excessively burdensome for the borrower, is subject, on conviction, to imprisonment for up to five years, or custodial arrest, or community service, or a fine not exceeding one hundred times the minimum monthly wage.

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132 Cabinet Regulation No. 692 of 25 August 2008 issued in accordance with Section 8, Paragraph 4 of the Consumer Rights Protection Law and Section 7, Paragraph 2 of the Advertising Law.
133 Ibid, Section 25
134 Criminal Code, Section 201
### Good Practice C.3

**Customer Records**

A bank should maintain up-to-date records in respect of each customer of the bank that contain the following:

- A copy of all documents required to identify the customer and provide the customer’s profile;
- The customer’s address, telephone number and all other customer contact details;
- Any information or document in connection with the customer that has been prepared in compliance with any statute, regulation or code;
- Details of all products and services provided by the bank to the customer;
- A copy of all correspondence from the customer to the bank and vice-versa and details of any other information provided to the customer in relation to any product or service offered or provided to the customer;
- All documents and applications of the bank completed, signed and submitted to the bank by the customer;
- A copy of all original documents submitted by the customer in support of an application by the customer for the provision by the bank of a service or product; and
- Any other relevant information concerning the customer.

A law or regulation should provide the minimum permissible period for retaining all such records and, throughout this period, the customer should be provided ready free access to all such records.

### Description

There is no law that covers all of these matters and minimum permissible time frames for retaining records vary according to the topic and applicable law.

For example, by Section 8 (5) 3) of the Consumer Rights Protection Law, banks must ensure the storage of all documents associated with the issuing of credit for one year after the fulfillment of the obligations specified in the consumer credit contract.

There is no provision in the Banks’ Code of Conduct that deals with these matters either.

### Recommendation

The law should be amended to require simple and consistent requirements as indicated above in respect of each customer for at least some years.

### Good Practice C.4

**Checks**

The regime regarding the issuance and clearing of checks must be based on clear statutory and regulatory rules that, among other things, set reasonable requirements for banks on the following issues:

- For any bank on which a check is drawn, when the account on which it is drawn has insufficient funds;
- For any bank at which a customer of that bank seeks to cash or deposit a check, which is subsequently found to be drawn on an account with insufficient funds;
- Informing the customer of the consequences of issuing a check without sufficient funds, at the time a customer opens a checking account;
- Regarding the crediting of a customer’s account and its timing, when a check deposited by the customer clears; and
- In respect of capping charges on the issuance and clearance of checks.

### Description

There is no existing regime of checks in the Latvian banking system. Rather, financial transactions occur in cash or by bank transfers made in person, written order or
### Good Practice C.5  
**Electronic Checks**

a. Customers should be provided with consistent, clear and timely information about electronic checks and the cost of using them, at all relevant stages in a consumer’s decision-making, in easily accessible and understandable form.

b. Customers should be informed:
   - (i) how the use of a credit card check differs from the use of a credit card;
   - (ii) of the interest rate that applies to the use of credit card check and whether this differs from the rate charged for a credit card purchase;
   - (iii) when interest is charged and whether there is no interest free period;
   - (iv) whether additional fees or charges apply and, if so, on what basis and the amount; and
   - (v) whether a purchase using a credit card check benefits from the same protection as using a credit card.

c. Credit card checks should not be sent to consumers without prior consent.

d. Authorities should encourage efforts to enable end users to better understand the market for electronic checks, such as providing comparative price information and undertaking educational campaigns.

e. There should be clear rules regarding procedures for error resolution.

### Good Practice C.6  
**Electronic Fund Transfers and Remittances**

a. There should be clear rules on the rights, liabilities and responsibilities of the parties in electronic fund transfers.

b. Banks should provide information on prices and service features of electronic fund transfers and remittances in easily accessible and understandable forms. As far as possible, this information should include:
   - (i) the total price (e.g. fees at both ends, foreign exchange rates and other costs);
   - (ii) the time it will take the funds to reach the receiver;
   - (iii) the locations of the access points for sender and receiver;
   - (iv) terms and conditions of the fund transfers services to the customer.

c. To ensure full transparency, it should be clear to the sender if the price or other aspects of the service vary according to different circumstances, and the bank should disclose the information without imposing requirements on the consumer.

d. There should be a legal provision requiring documentation of electronic fund transfers.

e. There should be clear, publicly available and easily applicable procedures in cases of errors and frauds.

f. Authorities should encourage efforts to enable end users to better understand the market for electronic fund transfers and remittances, such as providing comparative price information or undertaking educational campaigns.

### Description

The Bank of Latvia’s "Recommendations for Transactions Effected by Means of Electronic Payment Instruments" sets out minimum requirements for the issuance, service and use of...
electronic payment instruments (including payment cards, phone-banking applications, reloadable payment instruments and other similar instruments). The Recommendations prescribe general obligations and liabilities of credit institutions and their customers when conducting transactions by means of electronic payment instruments. The Recommendations establish minimum terms and conditions that should be communicated to the consumer prior to the consumer signing a contract for, or receiving, an electronic payment instrument.

Recommendation

No recommendation.

Good Practice C.7  Debt Recovery

a. No bank, agent of a bank or third party should employ any abusive debt collection practice against any customer of the bank, including the use of any false statement, any unfair practice or the giving of false credit information to others.

b. The type of debt that can be collected on behalf of a bank, the person who can collect any such debt and the manner in which that debt can be collected must be indicated to the customer of the bank when the credit agreement giving rise to the debt is entered into between the bank and the customer.

c. No debt collector should contact any third party about a bank customer’s debt without informing that party of: (i) the debt collector’s right to do so; and (ii) the type of information that the debt collector is seeking.

Description

Latvian debt collection agencies are unlicensed and operate without any regulatory oversight. As a result some existing agencies have been unscrupulous in harassing bank customer debtors. Aware, however, of the negative impact of such activity on their reputations, many banks are apparently insisting that their collection agents only employ fair and reasonable methods. That said, a delinquent debtor may experience what could reasonably be termed “undue pressure” from bank-appointed debt collectors.135

Given their un-regulated status, it is not surprising that no official statistics are available from collection agencies on any aspect of their activities.

Debt relief at a reasonable cost is essential for any individual unable to pay his or her debts as they come due over some reasonable period of time. Also, the law must grant all individuals and their banks the right to re-schedule debts. A working group under the supervision of the Ministry of Economy is drafting a new law on debt collection.

Recommendation

A Law on Debt Collection Operations would be helpful provided it would require, among other things:

a. the licensing and oversight of all properly registered collection agencies by an appropriate regulatory authority;

b. the provision of services in accordance with stated parameters on the basis of generally acceptable fair and reasonable behavior; and

c. the provision of statistics by each licensed agency to the regulatory authority on a regular basis for annual consolidation and wide-spread public dissemination.

SECTION D  PRIVACY AND DATA PROTECTION

Good Practice D.1  Confidentiality and Security of Customers’ Information

Customers have a right to expect that their financial transactions are kept confidential. The law should require banks to ensure that they protect the

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135 Although no studies have apparently been conducted on the social consequences of debt collection activities in Latvia, the adverse consequences are thought to be significant.
confidentiality and security of personal data, against any anticipated threats or hazards to the security or integrity of such information, and against unauthorized access.

**Description**

Latvia’s Criminal Code establishes sanctions against persons who commit violations of confidentiality of personal information.

“For a person who commits intentional violation of the confidentiality of personal correspondence or information in the form of transmissions over a telecommunications network, or commits intentional violation of the confidentiality of information and programs provided for use in connection with electronic data processing, the applicable sentence is deprivation of liberty for a term not exceeding three years or community service, or a fine not exceeding fifty times the minimum monthly wage, with or without deprivation of the right to engage in specific activities for a period not exceeding five years.” (Section 144).

Also, “for a person who commits intentional disclosure of personal confidential information of another person, if it has been committed by a person who pursuant to his or her position or employment must maintain the information entrusted or communicated to him or her in confidence, the applicable sentence is custodial arrest, or community service, or a fine not exceeding twenty times the minimum monthly wage.” (Section 145)

Please also see Section on Credit Reporting System, Good Practice A.1.

**Recommendation**

Please see Section on Credit Reporting System, Good Practice A.1.

**Good Practice D.2 Sharing Customer’s Information**

a. A bank should inform its customer in writing: (i) of any third-party dealing for which the bank must share information regarding any account of the customer, such as any legal enquiry by a credit bureau; and (ii) how it will use and share the customer’s personal information.

b. No bank shall sell or share account or personal information regarding a customer of the bank to or with any party not affiliated with the bank for the purpose of telemarketing or direct mail marketing.

c. The law should allow a customer of a bank to stop or “opt out” of the sharing by the bank of certain information regarding the customer and, prior to any such sharing of information, every bank should be required to inform each of its customers in writing of his or her rights in this respect.

d. The law should prohibit the disclosure of any information of a banking customer by third parties.

**Description**

Article 62 of the Credit Institutions Law states that information regarding a customer, his or her accounts and transactions, shall be provided to third parties only if the customer has unequivocally consented to provide such information with an agreement entered into with the credit institution. According to this Article, information regarding a client and his or her transactions, which is obtained by a credit institution when providing financial services in accordance with a contract, is “non-disclosable” information. Article 63 indicates cases where “non-disclosable” information shall be provided to another Member State or foreign institution, as well as the procedures that should be followed for this sharing of information. Voluntary or involuntary disclosure of this information is sanctioned by Article 64.

**Recommendation**

No recommendation.

**Good Practice D.3 Permitted Disclosures**

The law should:

a. State specific rules and procedures concerning the release to any government authority of the records of any customer of a bank;

b. State what the government authority may and may not do with any such records;

c. State what exceptions, if any, apply to these rules and procedures; and
d. Provide penalties for the bank and any government authority for any breach of these rules and procedures.

Description

The Credit Institutions Law in its Article 63 enumerates the State institutions and other government institutions that can obtain “non-disclosable” information of a customer of a bank, as well as the rules and procedures that govern the release of customer records to such institutions. Article 64 states that a person who discloses “non-disclosable” customer information (under circumstances described in this Article) shall be held criminally liable in accordance with the procedures specified by law.

Section 329 of the Criminal Code deals with “Disclosure of Non-disclosable Information” as follows:

“For a person who commits disclosure of non-disclosable information which is not an official secret, if commission thereof is by a State official who has been warned concerning the non-disclosability of the information or who, in accordance with the law, is liable for the storage of information, the applicable sentence is custodial arrest or community service, or a fine not exceeding twenty times the minimum monthly wage.”

Recommendation

No recommendation.

Good Practice D.4

Credit Bureaus

a. No credit bureau may begin or maintain operations without being licensed to do so by the appropriate government authority in accordance with the law.

b. Every bank must ensure the accuracy and credibility of the information it shares with any licensed credit bureau.

c. The law or regulations providing for oversight over credit bureaus should ensure that, amongst other things, the rules relating to consumer protection: (i) provide for the extent and timeliness of the updating of information regarding any bank customer; (ii) require that any bank customer’s records be kept confidential, except as may be expressly permitted by law; (iii) provide clear rules and procedures regarding the retention period of any credit record; (iv) require that every bank customer be informed in writing of the retention period; (v) require that every bank customer has ready, free access to all of his or her credit reports and be provided with a copy of any or all of his or her reports on conditions that are transparent; and (vi) provide procedures for correcting any mistake on a customer’s credit report.

Description

Please see Section on Credit Reporting System.

Recommendation

Please see Section on Credit Reporting System.

SECTION E

DISPUTE RESOLUTION MECHANISMS

Good Practice E.1

Internal Complaints Procedure

a. Every bank should have in place a written complaints procedure for the proper handling of any complaint from a customer, with a summary of this procedure forming part of the bank’s Terms and Conditions referred to in B. 7 above.

b. Within a short period of time following the date a bank receives a complaint, it should: (i) acknowledge in writing to the customer/complainant the fact of its receipt of the complaint; and (ii) provide the complainant with the name of one or more individuals appointed by the bank to deal with complaint until either the complaint is resolved or cannot be processed further within the bank.

c. The bank should provide the complainant with a regular written update on the progress of the investigation of the complaint at intervals of not more
than 10 business days.

d. Within a few business days of its completion of the investigation of the complaint, the bank should inform the customer/ complainant in writing of the outcome of the investigation and, where applicable, explain the terms of any offer or settlement being made to the customer/complainant.

e. When a bank receives a verbal complaint, it should offer the customer/complainant the opportunity to have the complaint treated by the bank as a written complaint in accordance with the above. A bank may not require, however, that a complaint be in writing.

f. A bank should maintain an up-to-date record of all complaints it has received that are subject to the complaints procedure. For each complaint, this record should contain the details of the complainant, the nature of the complaint, a copy of the bank’s response(s), a copy of all other relevant correspondence or records, the action taken to resolve the complaint and whether resolution was achieved and, if so, on what basis. The bank should make these records available for review by the banking supervisor or regulator as and when requested.

### Description

Detailed procedures for the processing of certain consumer claims are provided by Cabinet Regulation entitled: “Procedures for the Submission and Examination of Consumer Claims Regarding the Non-conformity of Goods or Services with Contract Provisions Issued pursuant to Section 27, Paragraph three of the Consumer Rights Protection Law”.  

These Regulations prescribe the procedures for the submission and examination of consumer claims regarding the non-conformity of goods or services with contract provisions and the organization of expert-examination of goods or services. The Regulation requires that sellers of goods and service providers submit written responses to consumers within 10 days of the time a complaint is submitted. However, this requirement does not apply to financial institutions. New amendments to the Consumer Rights Protection Law would require banks to respond within 30 days to consumer complaints related to debt restructuring and other specific matters.

Complainants typically complain in person or send their written complaints to the bank in question or to the CRPC, but there are apparently no standard requirements except as indicated above.

Most banks at least have customer relations units that exist to react to customer inquiries, but some apparently do not. While subsidiaries of some foreign banks track and catalogue complaints as they do in their head offices and branch offices overseas, no such practice apparently applies generally.

By the terms of the Banks’ Code of Conduct, banks are to provide an efficient customer complaint and dispute processing procedures so as to deal with customer complaints fairly and quickly. The Code also proposes that the customer have the right “to appeal a bank’s response to the complaint to the ombudsman of the Association of Latvian Commercial Banks” and “banks [are to] “respect decisions taken by the ombudsman regarding any consumer’s complaint”.

There is, however, nothing in the Code of Conduct dealing with the establishment of uniform standards in respect of the handling of delinquent debt, which is of course the prime reason any bank itself initiates a complaint against a consumer.

The extent of non-performing household loans on the books of Latvian banks is extraordinarily high by international standards. That is why the re-scheduling of these loans
Recommendations

Banks should be required by statute:

(i) to have in place a written complaints procedure for the proper handling of any complaint from a customer, with a summary of this procedure forming part of the bank’s General Terms and Conditions for any agreement with the customer;

(ii) to provide the customer with the name and address of an individual appointed by the bank to deal with the complaint until either the complaint is resolved or cannot be processed further within the bank;

(iii) to provide the complainant with a regular written update on the progress of the investigation of the complaint;

(iv) to inform the customer/complainant in writing of the outcome of the investigation within 30 days after first receiving the complaint;

(v) to explain in simple terms the nature of any offer of settlement being made to the customer/complainant;

(vi) to offer to have any verbal complaint of a customer treated by the bank as a written complaint in accordance with the above;

(vii) to maintain up-to-date records of all complaints it receives, including in respect of the nature of the complaint, a copy of the bank’s response(s), a copy of all other relevant correspondence or records, the action taken to resolve the complaint, and whether resolution was achieved and, if so, on what basis; and

(viii) to make these records regularly available for review by the CRPC or else on the request of the CRPC.

Furthermore, there should be a centralized system for the collection and recording of complaints, and these records should be made public, free of charge on the web, on a regular basis.

Good Practice E.2

**Formal Dispute Settlement Mechanisms**

a. A system should be in place that allows a customer of a bank to seek affordable and efficient recourse to a third party banking ombudsman or equivalent institution in the event the customer’s complaint is not resolved to his or her satisfaction in accordance with the procedures outlined in E. 1 above.

b. The existence of, and procedures before, the banking ombudsman or equivalent institution should be set forth in every bank’s Terms and Conditions referred to in B. 8 above.

c. The banking ombudsman or equivalent institution should be impartial and act independently from the appointing authority, the banking industry and the specific bank with which the complaint has been lodged.

d. The decision of the banking ombudsman or equivalent institution should be binding upon on the bank with which the complaint has been lodged and this fact, as well as the mechanism to ensure the enforcement of such a decision, should be set forth in every bank’s Terms and Conditions referred to in B. 8 above.

Description

If a consumer is of the opinion that a term of his or her contract with a bank is “unfair” under the terms of the Consumer Rights Protection Law or under those of the Unfair Commercial Practices Prohibition Law and yet the bank has either ignored or denied this allegation, the consumer has the right to file his or her claim with CRPC or the state court. In either event, the consumer will request a declaration that the offending term is “null and void”.

The Code of Administrative Procedure sets forth the requirements to commence and process a consumer’s action before the state courts.
The Law on Submission\textsuperscript{138} sets forth the procedures that must be followed by a consumer in any application to the CRPC, whether electronically\textsuperscript{139}, in writing or orally and whether by way of request, complaint, question or proposal.\textsuperscript{140}

Unless otherwise provided by the law, the CRPC is obliged to provide a reply to the consumer on the merits no later than one month following the receipt of the application.\textsuperscript{141}

If the CRPC makes a finding of unfairness, depending on whether the removal of the unfair term destroys the essence of the contract, the remaining contractual terms themselves may stand or fall (again as declared by the CRPC).

In addition, the CRPC has jurisdiction to act in these respects on its own initiative or on the basis of information provided by another institution.\textsuperscript{142}

The CRPC has the right to request all relevant information from the bank in question and to set the time-limit for the receipt of such information.\textsuperscript{143} And if information is not provided or is only partially provided within the time provided set by the CRPC, the CRPC is entitled to treat the information concerning the commercial practice as either “imprecise” or “false”.\textsuperscript{144}

On the basis of the “character and nature” of a commercial practice, the CRPC is entitled to propose that the bank ensure the conformity of the commercial practice with regulatory requirements within a specified time period; and undertake in writing to eliminate the breach, again within a specified time period.\textsuperscript{145}

If the CRPC is of the view that a commercial practice is illegal, it may decide that:

- the bank has to provide additional information to ensure conformity of commercial practices with the requirements of the Law;
- the bank must terminate the unfair commercial practice;
- the unfair commercial practice is prohibited, if it has not been commenced yet, but is anticipated (as, for example, being the subject of a clause in a draft contract);
- the bank must publish a notice that conforms with relevant commercial practice, in which the corrected information shall be specified by withdrawing the unfair commercial practices; or
- the bank is subject to administrative sanctions according to the procedures specified in the Law.\textsuperscript{146}

The maximum administrative sanction that can be applied to a bank by the CRPC is a fine of up to LVL 10,000 (i.e. approximately USD 20,000 equivalent).\textsuperscript{147}

The decision of the CRPC may be appealed to a court, but any such appeal does not suspend its application.\textsuperscript{148}

In case after case, the crucial test for the CRPC is whether specific language employed in a draft or existing contract is “unfair” in accordance with the terms of a relevant statute. In

\textsuperscript{138} Law on Submission, adopted by Parliament on 27 September 2007 and in force as of

\textsuperscript{139} Provided electronic signatures are employed. See ibid, Section 2 (3)

\textsuperscript{140} Ibid, Section 2 (1), The Law on Submission does not apply to requests for information.

\textsuperscript{141} Ibid, Section 5 (3)

\textsuperscript{142} See for example, Section 15 (1) of the Unfair Commercial Practices Prohibition Law

\textsuperscript{143} Ibid, Section 15 (2), Section 15 (1) of the Advertising Law provides for similar rights of the CRPC.

\textsuperscript{144} Ibid, Section 15 (3). See also Section 15 (2) of the Advertising Law for similar rights of the CRPC.

\textsuperscript{145} Ibid, Section 15 (4). By Section 15 (5), these rights do not prevent the CRPC from taking decisions referred to in Section 15 (8). See also Section 15 (3) of the Advertising Law for similar rights of the CRPC.

\textsuperscript{146} Ibid, Section 15 (8). For the CRPC’s decision-making power in respect of non-conforming advertisements, see Section 15 (4) of the Advertising Law.

\textsuperscript{147} See Section 26 of the Administrative Violations Code

\textsuperscript{148} Ibid, Section 16. See also Section 17 of the Advertising Law.
performing the *de facto* function of a first instance administrative tribunal as a result, the CRPC is therefore frequently required to apply complicated, arcane legal texts to specific contractual terminology.

Those in decision-making roles within the CRPC, however, appear to be less than adequately qualified given their lack of any, let alone sophisticated, financial services legal training.

Enough decisions, however, have emanated from the CRPC and the courts to give some indication of what are “unfair” contractual terms in banking practice.

As provided by the Consumer Rights Protection Law, of critical importance is whether the allegedly unfair contractual term has actually been mutually discussed and specifically agreed by the parties prior to the contract being signed. In these respects, it is important to note that the Courts and the CRPC have consistently taken the view that terms in standard contracts prepared by banks in advance are highly suspect as, *prima facie*, clauses that have not been mutually discussed. Also, the signing of an agreement containing a clause to the effect that all terms have been mutually discussed does not amount to irrefutable or sufficient evidence of this fact.

For the CRPC, it is essential that the consumer and a service provider’s employee actually exchanged ideas by email, in writing or otherwise regarding the specific contractual term which is the subject of complaint. Also, clear evidence of this fact must exist before the contract is signed.

As indicated above, Section 6 (3) of the Consumer Rights Protection Law provides contractual terms that are presumed to be unfair to the consumer.

In the first place, a contractual provision will be unfair if, in the event of a dispute, it purports to restrict a consumer’s right to make application to the CRPC or the State Court and seeks to have the consumer seek recourse only to the arbitration court. The Supreme Court of Latvia has resolved\(^{149}\) that an exclusive arbitration clause in a bank’s contract with a consumer will be unfair and therefore void unless the bank is able to prove that the clause had been separately negotiated and agreed with the consumer.\(^{150}\) It was also held that the signing of a standard contract afforded no evidence that any specific clause of the contract had in fact been negotiated with the consumer. The judgment, however, left open the question as to how a bank is to prove the required level of negotiation and mutual agreement.

Furthermore, the previous practice of providing the claimant the choice of recourse to the arbitration court of the Association of Latvian Commercial Banks or to the regular courts has also been termed “unfair” by the CRPC and the courts. In most consumer finance cases, of course, the bank will be the claimant seeking payment from the consumer/debtor and the bank will most likely therefore favor recourse to its Association’s arbitration court rather than the state courts. In all cases, the consumer must be the party choosing the dispute resolution forum although this, theoretically at least, could be the case if the consumer has, say by email, been given a single option by his or her bank in this respect (for, say, recourse only to the arbitration court) and the consumer then confirms acceptance to the bank by return of email.

In addition, a general contractual provision to the effect that the entire contract is subject to termination if the consumer does not fulfill his or her obligations is also unfair.

Although commercial banks and the Association of Latvian Commercial Banks would still like to have consumers as well as banks make recourse to the Association’s arbitration court or to *ad hoc* arbitration courts, the prevailing view of the CRPC and the

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\(^{149}\) See the final judgment of the Senate of the Supreme Court of Latvia dated March 2006 in Case no. SKA-59

\(^{150}\) In this respect, the Court was simply confirming the requirement of the Consumer Rights Protection Law that contract terms can be declared null and void if they are not mutually discussed and agreed prior to signing.
administrative courts is that these bodies have operated with inconsistent professionalism and have had conflicts of interest due to the power exercised by banks in appointing arbitrators and fixing all procedural rules in respect of arbitrations. The advice therefore that is apparently being consistently provided by legal advisors to Latvia's commercial banks is avoid contractual language that makes any reference to any arbitration court in Latvia.

In addition, pursuant to a Decision of the FCMC providing approval for recommendations regarding procedures for the out-of-court settlement of consumer disputes with credit institutions, an ombudsman has power to make non-binding recommendations to banks and consumers in the event a dispute arises between them but only in respect of a credit transfer or a transaction effected by an electronic payments system. This dispute resolution office, however, does not serve as a model for greater jurisdictional authority over consumer complaints for the simple reason that the existing ombudsman has, since 1 January 2003, effectively been appointed by the Association of Latvian Commercial Banks and is, at the same time, the Vice-President of this Association. Regardless of his bona fides in fact, therefore, his deliberations and recommendations are inevitably suspect in the minds of consumers.

At the European level FIN-NET is a financial dispute resolution network of national out-of-court complaint schemes in the European Economic Area countries (the European Union Member States plus Iceland, Liechtenstein and Norway) that are responsible for handling disputes between consumers and financial services providers, i.e. banks, insurance companies, investment firms and others. This network was launched by the European Commission in 2001.

Within FIN-NET, the schemes cooperate to provide consumers with easy access to out-of-court complaint procedures in cross-border cases. If a consumer in one country has a dispute with a financial services provider from another country, FIN-NET members will put the consumer in touch with the relevant out-of-court complaint scheme and provide the necessary information about it.

Neither the Association of Latvian Commercial Banks’ Ombudsman nor the Latvian Insurers’ Association's Ombudsman has joined the FINNET network, although Latvia has expressed its intention to the European Commission to encourage its ADR mechanisms to join the FINNET network.

### Recommendations

Consideration needs to be given to various options, including:

1. allowing the CRPC to make recommendations only;
2. allowing the CRPC to continue to make decisions but, in the event an appeal is taken within a short time frame following a decision, have the decision be suspended until a judgment is rendered by the administrative court of first instance or second instance (see below);
3. provide for appeals from any decisions of the CRPC directly to the second instance (i.e. appeals) court;
4. establish an office of financial services ombudsman, with jurisdiction over all types of consumer-related banking and other financial services disputes, and allow this office to make decisions that are binding on the parties (or at least binding upon the financial institution with which the complaint has been lodged) in the event the sum in question is less than a certain fixed level.

There should be a system in place that allows a customer of a bank to seek affordable and

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151 See Decision No. 311 (Minutes No. 42, p.3) of the Board of the FCMC dated 22 November 2002 and in force as of 1 January 2003.
152 The limited jurisdiction of the ombudsman has resulted in no more than some 10 cases per year being the subject of review since the inception of the office in 2003. And unfortunately, no record exists of the extent of success (i.e. how many recommendations have been voluntarily accepted by the parties).
efficient recourse to a third party (whether a financial ombudsman or equivalent independent institution) in the event that the customer’s complaint is not resolved to the customer’s satisfaction under internal procedures of the bank.

It should be a statutory requirement that the third party be impartial and act independently from the authority appointing the third party, the financial industry and the specific financial institution with which the complaint has been lodged.

And the decision of the independent third party should be binding upon the financial institution with which the complaint has been lodged.

Careful consideration should therefore be given to the establishment, by statute, of an office of Financial Services Ombudsman. And in this respect, existing models are worthy of analysis, including those of the EU generally and of Ireland, in particular, as an example of an EU Member-State.

Latvia should also consider whether it can push more strongly to join the FINNET network which would give its citizens better means of handling disputes across borders. This may be especially relevant to Latvians, as a large proportion may have financial products in other countries when working abroad.

### Good Practice E.3

#### Foreclosure

a. The law and related registry system should ensure an efficient process for the registration, public notice and ranking of secured interests on personal and real property of consumers.

b. When a consumer is in financial difficulty, the consumer’s bank should be ready to renegotiate the terms of a loan agreement with the consumer provided all terms are entirely fair to the consumer and not contrary to law.

c. In the event a renegotiation does not prove possible or the consumer is unable to meet his or her obligations under a revised loan agreement, the law should permit a fair and efficient process for the enforcement of any secured interest, including foreclosure on a mortgage, with rules of procedure in respect of the execution of judgments and the operation of bailiffs which are transparent and fair to the indebted consumer, as well as his or her bank.

### Description

The mortgage law and related registry system do ensure an efficient process for the registration, public notice and ranking of secured interests on personal and real property of Latvian consumers. This was highlighted in a recent publication from the EBRD\(^\text{153}\) which ranked the Latvian mortgage system as one of just three transition economies with a “very efficient” mortgage system, the other two being Lithuania and Slovakia.

The Financial Collateral Law\(^\text{154}\) is based upon Directive 2002/47/EC of the European Parliament and of the Council of Europe of 6 June 2002 on financial collateral arrangements and Directive 2000/12/EC of the European Parliament and of the Council of Europe of 20 March 200 on the business of credit institutions. This is augmented in large measure by more basics provisions of Latvia’s Civil Code. Also relevant is Latvia’s Land Registry Law. Among other things, this Law details the procedures for registering, as well as discharging, a mortgage.

And the existing Land Register, operated by the Land Registry Office, as well as the related Mortgage Registry, is classed as “state-of-the-art” and operates well, allowing ready public access to all pertinent up-to-date records for all concerned.


\(^{154}\) Adopted by Parliament on 21 April 2005.

The law provides that financial collateral may consist of cash or financial instruments and, on the occurrence of a so-called “enforcement event”, the collateral taker/creditor can realize any financial collateral according to the terms agreed in a security financial collateral arrangement. The law also contains close-out netting provisions and expressly states that they are applicable (i) even if insolvency proceedings are commenced against one of the counterparties, and (ii) notwithstanding any purported assignment, judicial or other attachment, or other disposition of or in respect of such rights.

Previously, if a consumer/debtor had agreed (in a financial collateral arrangement) to provide additional financial collateral to his or her creditor in the event that the value of his or her collateral had decreased, the provision of such additional collateral could not be declared invalid if it was provided prior to the publication of the announcement of the insolvency of the debtor (as provided for by the Insolvency Law and other regulatory enactments) or after the financial obligations guaranteed by the financial collateral had been incurred. As indicated below, however, following the recent amendments to the Consumer Rights Protection Law, protection has been afforded to mortgagors and their personal guarantors.

The Consumer Rights Protection Law's provisions on unfair contractual terms are now applicable to any natural person (often a relative, including next-of kin) who is a guarantor or provider of security for a consumer’s mortgage loan. Thus, if a guarantee agreement contains unfair contractual terms (in accordance with the Consumer Rights Protection Law), it is now possible to declare such an agreement or at least the certain separate offending provisions null and void, provided that the agreement is entered into with a natural person for the purposes of securing compliance with a consumer’s contractual obligations. In practice, however, it appears less than clear what kind of contractual terms can be considered unfair.

For example, the treatment of the guarantor is an especially important issue in Latvia given that this was a widely used form of security over recent years. As property prices rose, it seemed like a minimal risk for both the bank and the guarantor. Now that prices have collapsed any foreclosure actions often involve both the borrower and a guarantor whose property may also be at risk.

Although the guarantor is also subject to the Consumer Rights Protection Law, as stated above, it is not clear if they would be subject to the Regulations regarding Consumer Credit Agreements. It may well be the case that the guarantor signs a credit agreement without having received any form of advice or details of the loan repayment schedule which is being guaranteed. It is of course the responsibility of guarantors to take every precaution to ensure that they understand the risks they are facing, but it is clear that in the exuberance of the property boom, neither lenders, nor borrowers nor guarantors had much regard for the risks.

Finally, it is not clear whether the recent amendments dealing with guarantee agreements apply only to those concluded after 23 June 2009 or to any such agreements regardless of their date.

These most recent amendments also establish the right of a consumer or his/her guarantor...
to bring an action against the service provider for compensation by way of damages.

In addition, banks are now prohibited from requiring any consumer who has not committed “material violation” of the contract:

- to provide additional security in cases where a mortgage has lost its value due to depreciation in the real estate market;
- to cover the costs of a mortgage revaluation; or
- to accelerate repayment of a loan.

Material violation of the contract is considered to have occurred in cases where the borrower has: (i) delayed payment either of the principal amount or of interest by more than 60 days or by more than 30 days on more than three occasions annually; or (ii) utilized the loan for purposes other than those stated in the loan agreement.

Pursuant to the amendments, a consumer who has not committed a material violation of the contract at least once a year has the right to request his or her bank to consider a proposal for prolonging the repayment of the loan or a change in currency.

Finally, in cases where the CRPC has “reasonable suspicion” that the natural person in question is not a consumer (i.e. on the basis that he or she has acted for his or her business or for professional proposes), the CRPC now has the right to request that person to submit information (including information from the credit register regarding his or her obligations and information regarding his or her transactions) proving that he or she is, in fact, a consumer. Where that person fails to submit such information or that information proves unsatisfactory, the CRPC is not obliged to examine that individual’s complaint.

The CRPC therefore inevitably has significant on-going problems in interpreting the various above-mentioned statutory provisions.

But of greater concern, at least for creditors, is the difficulty faced in foreclosure actions pursuant to the Code of Civil Procedure. No out-of-court foreclosures are possible, other than a voluntary sale. And yet, once a court’s final judgment of foreclosure is entered and therefore ready for execution, the enforcement process can entail bailiffs organizing up to three separate auctions for the sale of the collateral property. The success rates of these auctions is very low with less than 10% of properties sold during first two auctions and less than half end up being sold at the end of the three auction cycle. If the property remains unsold, either the whole process has to be reinitiated or, more commonly, the bank agrees to take over the property with the borrower being allowed to stay in his or her home. The need for multiple auctions and various notice periods differ according to the value of the property but, in all cases, procedures are time-consuming, inefficient and costly. Present plans, however, call for reducing the time between auctions and abolishing an existing round of auctions, so the whole foreclosure process can become significantly smoother and more efficient, especially for properties valued at LVL 300,000 equivalent and above, where delays of up to 3 months between auctions remain the norm.\textsuperscript{158}

In addition, there are no guidelines by way of a “charter” or “protocol” which set out the expected behavior of banks and consumers in respect of one another in reaching possible out-of-court arrangements once a consumer loan, goes into default. Guidelines were developed for mortgage loans in 2009. The FCMC has published on its website the Principles and Guidelines for Out of Court Consumer Mortgage Workouts, prepared in cooperation with World Bank. However, it is not clear whether these Guidelines have been widely publicized so that consumers are aware of them.

Further complications exist with the auction process such as the need to publish an announcement of the auction in an official journal which inevitably delays the process and

\textsuperscript{158} A delay of three months between auctions apparently does not amount to an intentional delay in the execution of a court judgment or decision which, by the terms of Section 296 of the Criminal Code, would subject the bailiff/perpetrator to a fine of up to 60 times the minimum monthly wage.
incurs further expense. Secondly, the purchaser of the property at the auction has a relatively short settlement period within which to make the payment. This generally means that the purchaser is unable to arrange a mortgage loan in advance of the auction, thereby limiting the number of potential buyers able to participate in the process.

As currently designed, the auction process is long and cumbersome for both the borrower and the lender. It serves neither party particularly well in obtaining the best value for the property. The initial value of the property is ascertained under conditions of forced sale which results in a lower valuation than in an open market. And this can be further reduced if the sale goes to the third auction where the reserve price is set at 60% of the forced sale price. This can mean that the property ends up being sold at less than 50% of its open market value. In addition, this sale may well take place over a year after foreclosure proceedings have been initiated. At the current levels of property price deflation, this would mean a further 60% drop in the value. The net impact is to make foreclosures very much of a last resort for both banks and consumers.

Debt relief at a reasonable cost is essential for any individual unable to pay his or her debts as they come due over some reasonable period of time.

**Recommendations**

While the existing secured transactions legislation does not now warrant amendment and there is no need for a new law on mortgages, as indicated above, standard-form contracts, or at the very least standard fair specific terms, for consumer loans, including mortgage loans, should be prepared by the CRPC in close collaboration with the Association of Latvian Commercial Banks and these should then be formally endorsed by the Association, all individual Latvian commercial banks and the CRPC.

In addition, a "Protocol" or "Charter" should be prepared by the NGO community with strong support from the Latvian Government that sets out the expected behavior of banks and consumers regarding one another in reaching out-of-court arrangements when any consumer loan is in default. This Protocol or Charter should then be formally endorsed by the Association of Latvian Commercial Banks, all individual Latvian commercial banks and the CRPC. Although voluntary in nature, the application of the Protocol would allow the consumer to resolve his or her debt problems in a way that would afford a greater degree of certainty than would be the case if the dispute were resolved in the courts and a subsequent auction process undertaken as a result. If a consumer does not adhere to the Protocol, he or she would effectively be waiving his or her rights to having a debt work-out. It may also affect the way the consumer is dealt with in court if he or she is seen as being unwilling to behave reasonably.

For banks, a Protocol is likely to be complied with since the restructuring of debt will typically be much cheaper than going to court and from there through the auction process in an effort to seek legal foreclosure. As indicated above, foreclosure is invariably the last resort for any bank since no bank usually recoups its costs in the process. Also, provided the Protocol is sponsored as an important initiative of the Latvian Government and receives maximum publicity, a bank’s reputation will likely suffer significantly if it either refuses to endorse it or does not abide by its terms in contravention of its endorsement.

In addition, ongoing efforts to amend the Code of Civil Procedure, including in respect of the execution of judgments and the law dealing with the operations and fees, etc., of bailiffs should be strongly encouraged in order to improve the capacity and efficiency with which foreclosure procedures are effected and the immovable property in question is sold at auction.

Finally, in order to promote legal certainty, it would help considerably if, following the example of the European Union, the CRPC were to issue guidelines regarding the kind of contractual terms in mortgage (and other consumer) loans that are considered "unfair".
<table>
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<th>Good Practice F.1</th>
<th>Depositor Protection</th>
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<tbody>
<tr>
<td>a. The law should ensure that the regulator can take prompt corrective action on a timely basis.</td>
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<td>b. The law on deposit insurance should be clear on:</td>
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<td>(i) the insurer;</td>
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<td>(ii) the classes of those depositors who are insured;</td>
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<td>(iii) the extent of insurance cover;</td>
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<td>(iv) the holder of all funds for payout purposes;</td>
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<td>(v) the contributor(s) to this fund;</td>
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<td>(vi) each event that will trigger a payout from this fund to any class of those insured; and</td>
<td></td>
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<tr>
<td>(vii) the mechanisms to ensure timely payout to depositors who are insured.</td>
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<tr>
<td>c. In the absence of deposit insurance, there should be an effective and timely payout mechanism in the event of insolvency of a bank.</td>
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<tr>
<th>Description</th>
<th>The EU Directive on Deposit Guarantee Schemes (94/19/EC) has been transposed into Latvia's Deposit Guarantee Law.(^{159}) And, following agreement reached on October 7, 2008 by the Economic and Financial Affairs Council of the European Union, deposit guarantee protection was increased from €20,000 to €50,000.(^{160})</th>
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<td>The Deposit Guarantee Law provides for a deposit guarantee fund which is accumulated and managed by the FCMC.(^{161}) The responsibilities of the FCMC are to:</td>
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<td>a) pay out deposit compensation amounts to insured depositors(^{162}) on the occurrence of an &quot;insured event&quot;;</td>
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<td></td>
<td>b) keep and update a register of banks and credit unions that participate in the Deposit Insurance scheme;</td>
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<td>c) monitor the formation and maintenance of the deposit insurance fund, including the insurance premiums of banks; and</td>
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<td></td>
<td>d) manage the resources of the deposit insurance fund.</td>
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<td>The trigger for the payment to depositors is the &quot;unavailability&quot; of insured deposits, as defined in the Deposit Guarantee Law. Insured deposits are &quot;unavailable&quot; when the license of the credit institution has been revoked by the FCMC in accordance with Article 27 of Credit Institutions Law. In accordance with Article 129 of the Credit Institutions Law, when the license has been revoked by the FCMC, the FCMC must appoint a so-called &quot;authorized person&quot;, submit to a court an application for the liquidation of the credit institution and appoint a liquidator. By Article 20 of the Deposit Guarantee Law, the authorized person so appointed is then required to make payments of the insured deposits to the depositors within twenty working days from the date deposits becomes unavailable, i.e. when the license was revoked.</td>
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<td></td>
<td>In the event that deposits in the deposit insurance fund prove to be inadequate, the shortfall is made up by means of payments from the Government budget to FCMC.(^{163}) Thus, the ultimate insurer is the Government of Latvia.</td>
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\(^{159}\) In force as of 1 October 1998, as amended.  
\(^{160}\) By Article 3 (1) of the Deposit Guarantee Law, the limit of EUR 50,000 is "translated into Latvian lats at the Latvian Central Bank's exchange rate effective on the day when the event of non-availability of deposits occurred."  
\(^{161}\) As of July 2008, LVL 77.7 million (i.e. about USD 155 equivalent) has been accumulated in the Fund.  
\(^{162}\) By Article 16) of the Deposit Guarantee Law, a "depositor" is defined as "a person who has a guaranteed deposit with a deposit taker." The term "person" covers both natural and legal persons.  
\(^{163}\) See Article 15 (1). So far at least, however, there has been no need to call on any non-Fund deposits.
The Guarantee Fund is made up of quarterly payments from deposit takers (i.e. banks, branches of foreign banks and credit unions) as specified in the Deposit Guarantee Law, single payments from the Government’s budget and the Bank of Latvia, as well as income forthcoming from the management of the Fund. In addition, the Fund is supplemented by a single payment of LVL 50,000 made by any new bank when obtaining an operating license and a single payment of LVL 100 made by each credit union.

The trigger is the “unavailability of deposits” which prevents the deposit taker from paying out the guaranteed deposit as determined by the FCMC. No application is required on the part of the consumer or of the deposit taker. Rather payments are made in automatically as a result of “the data available in the accounting registers of the deposit taker on the day of the occurrence of unavailability of deposits.” The deposit taker is obliged to keep an up-to-date list of all depositors to which guaranteed compensation is to be paid out and to provide this list to the FCMC within one day after the occurrence of “Unavailability of funds”. Payments are then required to be made within 20 working days from the date of the occurrence of the unavailability of deposits.

If a depositor has more than one account with the same deposit taker, all accounts are added together and treated as one account.

### Recommendations

Careful review is now underway regarding proposed amendments to the Credit Institutions Law and the Code of Civil Procedure which, once enacted and applied, would strengthen the Latvian legal framework for bank insolvency in general. The amendments to the Credit Institutions Law would in particular strengthen the powers of the FCMC to take prompt corrective action, in particular, in the event financial difficulty is faced by any Latvian bank or branch in Latvia of a foreign bank. The various amendments in both instances should be enacted at the earliest opportunity. There are, however, still further matters deserving of attention, including the need for a comprehensive review of the legal framework for bank resolution in order to improve upon its internal logic. While a special committee within the FCMC has been established to deal with the management of the deposit guarantee fund, including all pay out procedures in the event of the failure of any credit institution, it is essential that this committee has appropriate financial resources, skilled personnel and internal control systems.

Matters for FCMC consideration include:
- accomplishing measures aimed at better ensuring the preservation of any failed bank’s property and documents;
- expanding the range of possible legal actions available in order to bring to account persons whose actions or omissions have contributed to the bankruptcy of a bank; and
- better defining the methods and forms of government involvement in dealing with banks facing financial difficulties.

It is also recommended that close consideration be given to the application of Principles 14, 15, 17, 18, 20 and 21 from the [Core Principles for Effective Deposit Insurance Systems](http://www.iadi.org/docs/Core_Principles_final_29_Feb_08.pdf) as produced by the International Association of Deposit Insurers (IADI). The IADI was established in 2002 to enhance deposit insurance effectiveness by promoting guidance and international cooperation.

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164 Ibid, Article 7. An initial payment of LVL 0.5 millions was made to the Fund by the Government and an equivalent sum was paid in by the Bank of Latvia.

165 For example, in 2007, Fund income amounted to an additional LVL 2.4 million which was as a result of investments by FCMC of Fund assets in Government treasury bills.

166 Article 1 (5) (c) of the Deposit Guarantee Law

167 Article 14 (1)

168 Article 14 (2)

169 Article 20 (1). By Article 20 (2), on an exceptional basis, not more than an additional 10 working days may be allowed.

170 The IADI’s Core Principles for Effective Deposit Insurance Systems are particularly helpful and available at http://www.iadi.org/docs/Core_Principles_final_29_Feb_08.pdf.
### Insolvency

a. Depositors should enjoy higher priority than other unsecured creditors in the liquidation process of a bank.

b. The law dealing with the insolvency of banks should provide for expeditious, cost effective and equitable provisions to enable the maximum timely refund of deposits to depositors.

### Description

The rules regarding bankruptcy proceedings for credit institutions (i.e. commercial banks) are set forth in Chapter XIV of the Credit Institutions Law. As the Law makes clear: "The basic purpose of bankruptcy proceedings is to gain maximum income from the sale of the property of a credit institution, thereby ensuring the satisfaction of creditors' claims as fully as possible".\(^1\)

Immediately after payment of the cost of insolvency proceedings, the funds remaining are distributed, for the satisfaction of the principal sum of creditors' claims, in the following order of priority:

1. payments to depositors who are entitled to a guaranteed compensation;
2. claims of employees for salary for the last three months of employment in the 12 month period prior to the court judgment declaring the credit institution insolvent;
3. taxes and other debts to the State budget and the budgets of local governments;
4. debts to creditors which have arisen from a credit institution accepting, but failing to fulfil, payment orders from a client regarding money transfers to the State or local government budgets; and
5. State claims regarding repayment of credits guaranteed by the State.\(^2\)

Thus, depositors do enjoy higher priority over other unsecured creditors in the liquidation process of a bank.

After satisfaction of creditors' claims as provided above, the remaining funds are then distributed for the satisfaction of creditors' claims in the following order of group priority:

1. the remaining legal claims of the creditors (principal sums without interest), including claims of those who may have obtained creditor status after the initiation of insolvency proceedings, to the extent they are not treated as claims provided for above, deferred tax payments after payments provided for above, the remaining deposits of natural persons and salary debts, as well as other payments arising from lawful employment relations, shall be treated as if they were claims of this group. If a creditor's deposit has been insured and the creditor has received insurance compensation, the claims of the relevant insurance company (fund) against the credit institution shall be treated as if they were claims of this group;
2. claims regarding interest payments to creditors;
3. claims of such creditors who have submitted their claims after the specified time limit; and
4. claims regarding the funds which creditors have loaned to the credit institution for a definite period, with the condition that repayment may be requested before the expiration of such time period in the case of the credit institution's liquidation.\(^3\)

Anyone who is connected with an insolvent credit institution who intentionally grants unjustified priority rights to any creditor, or agrees that such rights be granted, is subject to administrative or criminal liability.\(^4\)

The claims of each subsequent group of creditors are satisfied only after complete satisfaction of the previous group of creditors. If the funds of the credit institution are

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\(^1\) See Section 185 (1) of the Credit Institutions Law
\(^2\) Ibid, Section 192
\(^3\) Ibid, Section 193
\(^4\) Ibid, Section 200
inadequate to satisfy all claims of the creditors of one group, such claims shall be satisfied proportionately to the amount due to each creditor within the group.\textsuperscript{175}

Finally, any funds which remain after the satisfaction of the claims referred to above are then distributed to the shareholders of the credit institution proportionately to the amount of the contribution of each.\textsuperscript{176}

On paper at least, the law would seem to provide expeditious, cost effective and equitable provisions to enable the maximum timely refund of deposits to depositors. No information has been obtained, however, regarding experience to date in applying and enforcing these provisions.

It is important to note that two extensive reviews of the legal framework for bank resolution have recently been carried out. These have resulted in numerous amendments to the Credit Institutions Law, as well as the Code of Civil Procedure. The purpose has been to strengthen the Latvian legal framework for bank insolvencies by making the process more expeditious, cost effective and equitable.

Recommendation

No recommendation.

\textbf{SECTION G CONSUMER EMPOWERMENT}

\textbf{Good Practice G.1 Financial Education in Schools}

Information about basic financial products, such as current and deposit accounts, leasing contracts, term loans and mortgages and credit cards, as well as how to calculate and compare interest rates, should be taught in schools. Schools should also teach basic financial concepts such as risk vs. return, long-term financial planning and consequences of over-indebtedness.

\textbf{Description}

The public school curriculum does not include the topic of financial education at any level. The elementary school subjects "Introduction to Economics", "Social Science and Home Economics and Technology" and the secondary school subjects "Fundamentals of Business Economics" and "Politics and Law" indirectly include some information on consumer protection and financial and economic issues, but there are no topics focused on financial education or financial consumer protection. No materials related to these issues are available and teachers have no adequate training to teach with understanding and authority about them.

Money Planning Centre, an organization created by GE Money in 2007 with the objective of educating consumers on financial planning and other financial matters, has recently published a book that explains basic financial issues in simple terms. Money Planning Centre has signed a Memorandum of Agreement with the agency that oversees libraries in Latvia, in order to distribute the book for free in all libraries. This project was financed by GE Money and the insurance company If Latvia. The Ministry of Education has apparently shown interest in this material. Money Planning Centre has conducted other activities focused on educating children regarding financial issues, such as a competition for children in 1\textsuperscript{st} to 4\textsuperscript{th} grade based on paintings of what children understand about money.

The Consumer Protection Policy Guidelines of 2004 are recognized as one of the main guiding principles for consumer policy. By these Guidelines, consumers are to be provided with consumer protection information, as well as consumer education in schools.

The Consumer Protection Program for 2005-2007 included as a focus area the provision of information on consumer protection and promotion of consumer education. One of the activities developed under this area was the project “Prudent Borrowing”, a competition for secondary school students regarding responsible consumer credit (e.g. how to spend LVL

\textsuperscript{175} Ibid, Section 194
\textsuperscript{176} Ibid, Section 195
100 wisely?), organized in 2007. The activity was funded by the CRPC and organized by the umbrella consumer association PIAA, with support from Money Planning Centre. The contestants were evaluated by a committee of experts from non-governmental organizations, the Ministry of Economics, the Association of Latvian Commercial Banks, Money Planning Centre, and GE Money.

<table>
<thead>
<tr>
<th>Recommendation</th>
<th>The Ministry of Education should consider the inclusion of topics on financial education in the public school curriculum.</th>
</tr>
</thead>
</table>

### Good Practice G.2 Financial Education through the Media

| a. | Print and broadcast media should be encouraged to cover issues related to retail financial products. |
| b. | Regulators and/or industry associations should provide sufficient information to the press and broadcast media to facilitate analysis of issues related to financial products and services. |

### Description

There are 2 main newspapers specialized in financial news (one in Latvian and one in Russian). In addition, some financial articles have recently been included in weekly general magazines such as Ieva.

Two TV stations (LTV and TV3) broadcast daily shows based on real complaints that Latvian people share with the TV stations about different types of products or services. In the last months, there has been an increase in the number of complaints regarding financial products or services that are presented and discussed in the shows. These shows usually invite an officer of the CRPC and/or FCMC to provide comments on the complaints. In addition, the Bank of Latvia sponsors a TV show dealing with news on economic and financial issues.

On the radio, Latvian Radio Station’s show "Ka labak dzivot?” or "How to live a better life?” also touches upon financial issues and calls experts from institutions like the CRPC or Money Planning Centre to ask their opinions.

<table>
<thead>
<tr>
<th>Recommendation</th>
<th>There is some participation of regulators in the media to facilitate analysis of issues related to financial products and services. However, there could be improvements in the frequency and detail of information given by regulators to the media and from the media to the public.</th>
</tr>
</thead>
</table>

### Good Practice G.3 Information Resources for Consumers

| a. | Financial regulators should seek to improve consumer awareness of financial products and services by devising, publishing and distributing independent information on the costs, risks and benefits of such products and services. |
| b. | Non-governmental organizations should be encouraged to provide consumer awareness programs to the public regarding financial products and services. |

### Description

In order to raise public awareness on issues related to central bank activities, the Bank of Latvia created “Money World” as a financial education and information center. Money World began its operations in February 2005. The displays in Money World have been organized considering a target population of school students older than 14 years with some preliminary knowledge. However, the contents of the displays are easy to understand for anybody interested in issues related to monetary policy, circulation of money, history and money, and for those who want to make more informed decisions in their own financial matters. On average, some 600 people visit Money World every month. However, FCMC does not publish general information to improve consumer awareness of financial products and services. There is no provision of information on costs, risks and benefits of financial products and services.

Money Planning Centre has developed a program application (Naudas Konotroleris or Money Controller) to be downloaded to mobile phones, with the objective of helping a consumer planning his or her personal budget. The application allows a person to register a controlled personal cash flow (known income minus planned expenses), record each purchase on a daily basis and analyze expenses and balance of planned income. In addition, Money
Planning Centre has organized a series of seminars or panels that go to different cities and villages within the country and talk about financial issues. The Money Planning Centre receives the support of local institutions in order to reach a higher audience of consumers. In addition, the Money Planning Centre’s website http://vissparnaudu.lv provides consumers with information on several financial issues.

The Banking Academy has also engaged in some consumer awareness activities. The Academy has conducted conferences and seminars and, in 2007, sponsored a project developed by students, which resulted in a booklet describing key information on mortgage credit for the average consumer (Kas ir kredits).

**Recommendation**

FCMC could provide more information on financial products and services to improve consumer awareness.

Consumer associations should be more involved in the development of consumer awareness programs on financial issues in the Riga area and in other regions of Latvia.

**Good Practice G.4**

**Financial Consumer Advocacy**

In the development of financial sector policy, government and state agencies need to consult with banks and consumers and their respective associations in order to develop proposals that meet the needs and expectations of these key stakeholders. To ensure that consumers are actively involved in the policy development process, the government, or private sector organizations, should either provide appropriate funding to non-governmental organizations for this purpose or create a special entity to lobby on behalf of consumers in the policy-making process.

**Description**

There is one umbrella consumer organization in Latvia (PIAA), which currently groups some 10 consumer associations (or "clubs") and tenant organizations. Consumer Guide, established in 1991, is the oldest consumer club in Riga. The second oldest is Consumer Support Centre, with 15 years of operation. PIAA was established in 1999.

However, all consumer organizations in Latvia have faced severe problems in terms of financial resources. There has never been any (let alone any major) stable source of funds for their activities. Only once, in 2007, the government provided funds for their development (LVL 30,000 assigned by the CRPC). However, this limited funding was given to the umbrella organization, which later re-distributed the funds among the different associations based on perceived "necessities" for several projects.

Besides direct allocation of government funds, the other potential source of finance for consumer associations is the EU. However, a pre-condition of EU financing has been co-financing from the government, which has been difficult to obtain according to the consumer associations.

The consultative council on consumer protection was set up in order to ensure the direct participation of consumer associations and other stakeholders in the process of policy-making regarding consumer issues. However, the last time the council met was in 2008 and there is no plan to reactivate it in the near term.

Given the difficult financial situation of all consumer organizations, other institutions are developing an advocacy role for consumers. The Banking Academy School of Business and Finance is an educational institution that was originally created and funded by the Bank of Latvia. This School later became self-sustainable (under the Ministry of Education). Banking Academy has developed a series of educational programs on financial issues (including graduate programs), conducted seminars and trainings on banking and financial issues, and developed research projects (in 2007 the Banking Academy also funded the BA Research Centre, which is a non-governmental organization focused on research in financial matters. In December 2008, the Banking Academy organized a conference on the need of a strategy to improve financial literacy in Latvia.

Since its creation in 2007, the Money Planning Centre has been conducting several activities
to improve consumers’ understanding of financial issues throughout the country. In addition, the Money Planning Centre has shown interest in policy advocacy for consumers. For example, in 2007 the Money Planning Centre proposed to include a warning phrase on responsible lending in all advertising related to financial products. This proposal was taken-up by the CRPC, and the Cabinet of Ministries issued a Regulation on responsible credit at the end of 2007, which has since required all relevant advertisements to include a phrase along the lines of “Don’t forget to borrow in a responsible way”. Recently, the Money Planning Centre has also been advocating the need for a national strategy for financial education in Latvia, as well as the publication of materials on financial issues for schools.

**Recommendation**

Consumer associations should play a key role in financial consumer protection. They are generally the first place consumers go for advice and information, especially in remote areas of the country. Consumer associations should be allies of the government’s consumer protection agency in the task of protecting consumer rights. Consumer associations need adequate and stable sources of funding, but also adequate institutional capacity that allows them to manage funds efficiently and provide a good service to consumers.

There is need for the development of institutions that are able to provide advocacy for financial consumers in the policy-making process. The consultative council for consumer protection should be reactivated in order to have an official forum for discussion of policies with representatives of consumers.

The government should provide consumer associations with stable funds to promote their operations. In a context of limited resources, the government should be ready to help consumer organizations obtain funds from the EC on the basis of specific projects, providing the minimum required co-financing for this matter. At the same time, consumer organizations should improve their transparency, accountability and management efficiency, especially if they are to receive government funding. They should each publish an Annual Report describing the results of their activities and their impact on consumers and make these Reports publicly available.

**Good Practice G.5 Measuring Financial Capability**

In order to ensure that financial consumer protection, education and information initiatives are proportionate and appropriate, and in order to measure the effectiveness of those initiatives over time, the financial capability of consumers should be measured periodically by way of large-scale market research that gets repeated from time to time. For these purposes, the term “financial capability of consumers” means the ability to manage money, keep track of finances, plan ahead, choose appropriate financial products and services and stay informed about financial matters.

**Description**

In 2006, GE Money developed a study to understand consumer attitudes towards, and experiences with, consumer credit. This project consisted of focus group discussions and a large survey. Latvia Facts, a sociological and market research centre, was in charge of these activities. The survey of attitudes and experiences was conducted in February 2006. The results showed that 46 percent of the surveyed population (1,007 respondents) recognized their inadequate knowledge relating to consumer credit issues, despite the fact that 55 percent of respondents thought that consumer credit agreements were generally uncomplicated and comprehensible. Regarding the conditions to obtain consumer credit, 73 percent considered the application process to be easy and fast, 72 percent considered that required information was available and sufficient, and 73 percent considered that credit institutions offered flexible terms in consumer loans.

The survey also showed that respondents were most familiar with interest rate information (95 percent) and penalty interest (89 percent) in respect of their loans. However, only 63 percent were familiar with dispute settlement options.

A third of the population (31 percent) had been granted consumer credit during the year before the survey. The main reasons why respondents had not used consumer credit were: no need of credit (36 percent), high interest rates (26 percent) and low salary or unsteady income (15 percent). The main socio-demographic group that sought and received
consumer credit consisted of people from 25 to 39 years of age with higher education, relatively high monthly income per family member and with children, if any, of less than 15 years old. Respondents who had already been granted consumer credit were planning to continue having consumer credit for 12 more months. Only one in ten of the respondents who had not been granted consumer credit was willing to take credit in the following year.

Besides this initial survey of consumer understanding of financial issues, there has been no initiative to measure the level of financial capability of consumers in Latvia.

**Recommendation**

A nationwide financial literacy survey would permit the authorities to measure the financial capability of consumers. This information would allow better prioritization and targeting of measures for purposes of financial education, especially in the context of limited resources. The survey would provide baseline information before the implementation of specific measures. Some years afterwards, a second survey would measure the effectiveness of the initial initiatives undertaken so that course-correction would follow, as appropriate.

### SECTION H

**SECT**

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**COMPETITION AND CONSUMER PROTECTION**

<table>
<thead>
<tr>
<th>Good Practice H.1</th>
<th>Regulatory Policy and Competition Policy</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Description</strong></td>
<td>Financial regulators and competition authorities should be required to consult with one another for the purpose of ensuring the establishment, application and enforcement of consistent policies regarding the regulation of financial services.</td>
</tr>
</tbody>
</table>

Notwithstanding the fact that the FCMC is responsible for ensuring free competition within the financial and capital markets and the Competition Council is charged with enforcing the Law on Competition which applies to all sectors of the Latvian economy, including the delivery of financial services, there is nothing in the law to require any, let alone regular, consultations among these institutions and the CRPC, so as to ensure consistency in establishing, applying and enforcing financial services regulations. *Ad hoc* consultations apparently do, however, take place among the Competition Council, the FCMC and the CRPC to discuss issues of common concern but meetings of this sort are rare.

It is noteworthy that the Criminal Code imposes a term of imprisonment of up to two years or community service, or a fine not exceeding 100 times the minimum monthly wage, with or without deprivation of the right to engage in entrepreneurial activity for not less than 2 years and not more than 5 years, for any person who fails to comply with the legal requirements set out by a State institution for the protection and encouragement of competition if the commission of such offence is repeated within one year or if it causes substantial harm to the interest of the State or of consumers.\(^{177}\) (Emphasis added.)

Also, by the terms of the Criminal Code, a person who commits unfair competition (or misleading advertising), if commission of such offences is repeated within a one-year period, is, on conviction, subject to imprisonment for a term not exceeding two years, or community service, or a fine not exceeding eighty times the minimum monthly wage, with or without deprivation of the right to engage in entrepreneurial activity for a term of not less than two years and not exceeding five years.\(^{178}\)

**Recommendation**

The Competition Council, the FCMC and the CRPC should consult regularly with one another so as to ensure the establishment, application and enforcement of consistent policies regarding the regulation of financial services.

<table>
<thead>
<tr>
<th>Good Practice H.2</th>
<th>Review of Competition</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Given the significance of retail banking to the economy as a whole and to the welfare of consumers, competition authorities should:</strong></td>
<td></td>
</tr>
<tr>
<td>a. Maintain a watching brief on competition in retail banking; and</td>
<td></td>
</tr>
</tbody>
</table>

\(^{177}\) See the Criminal Code, Section 212

\(^{178}\) Ibid, Section 211
| **Good Practice H.3** | **Licensing of Legal Entities**  
All legal entities that either collect funds from consumers or lend funds to consumers should be licensed and supervised. |
|----------------------|------------------------------------------------------------------------------------------------|
| **Description**      | According to the law, all legal entities that collect funds from consumers should be licensed by the FCMC. However, there is an exception for certain electronic money institutions. By amendments to the Law on Credit Institutions (with effect from November 2004) the establishment of the “electronic money institution” as a new type of credit institution was first allowed. The law, however, also includes certain exceptions (set out in the E-money Directive) that permit the establishment of electronic money institutions **without a license** from the FCMC if the electronic money institution does not plan to issue more than €5 million equivalent in electronic money (and the stored electronic money in one of its storage device does not exceed 150 euro equivalent in lats).  
A concept document has been approved by the Government, indicating that entities lending funds to consumers will have to be licensed by the CRPC. |
| **Recommendation**   | All legal entities that either collect funds from consumers or lend funds to consumers should be required to be licensed to operate, and then supervised (preferably by the FCMC). As minimum, financial institutions that do not collect funds from consumers should be subject to business conduct supervision. |
Latvia: Consumer Protection in the Non-bank Credit Institutions Segment

Overview

The segment of non-bank credit institutions\(^{179}\) (NBCI) in Latvia is dominated by leasing companies. The NBCI segment comprises financial institutions engaged in lending activities, such as credit unions and credit cooperatives, and other financial institutions such as leasing and factoring companies and pawn shops. The segment of NBCI is largely dominated by leasing companies, which represented about 62 percent of NBCI assets by December 2008. However, the market share of leasing companies within the NBCI segment decreased ten percentage points compared to the levels of 2006 and 2007 (Figure 6). Total assets of the NBCI segment reached LVL 3,192 million by end-2008, almost ten times higher than the level in 2001. By December 2008, the NBCI segment represented 12 percent of the total assets of the financial sector, 5 percentage points higher than the market share in 2004.

![Figure 6: Structure and Level of NBCI Assets](image.png)

Source: Bank of Latvia

From 2001 to 2008 the assets of NBCIs grew more than those of the banking sector and the overall financial sector. The assets of the NBCI segment grew at an average annual rate of 44 percent from 2001 to 2008. The assets of the banking sector and the entire financial sector grew at a similar average annual rate of 34 percent (see Figure 9). The total assets of the financial sector amounted to LVL 27,046 million by end 2008, while the assets of the banking sector amounted to LVL 23,243 million.

\(^{179}\) The EC Capital Requirements Directive 2006/48 defines credit institutions as undertakings whose business is to receive deposits and other repayable funds from the public and to grant credit for its own account; non credit institutions are defined as undertakings which are active in the financial sector but are not registered as credit institutions according to domestic regulation.
Leasing Sector

The leasing sector in Latvia is represented by 23 leasing companies whose main customers are private companies. The activities of leasing companies cover financial and operational leasing, factoring operations as well as consumer lending. However the statistical information of the leasing sector that is currently collected and published by the Bank of Latvia does not allow identifying the different financial products offered by leasing companies. According to the Bank of Latvia, non-financial private companies are the main recipients of credit by leasing companies. However credits to households have increased their participation in the leasing credit portfolio from 14 percent in 2005 to 20 percent in 2008.

The increase of credit to households by leasing companies has been driven by products other than consumer or housing credit. While in 2005 about 70 percent of the credits to households was in the form of consumer credit, in 2008 this percentage decreased to only 37 percent. At the same time, the share of credit for housing purchases has remained at a small level (around 1 percent) throughout 2005-2008. In contrast, other credits to households increased their participation from 29 percent in 2005 to 69 percent in 2008.

Table 5: Credit Portfolio Structure of Leasing Companies
(in percentage)

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>Credit to private non-financial sector</td>
<td>80.1</td>
<td>77.8</td>
<td>77.8</td>
<td>71.1</td>
</tr>
<tr>
<td>Credit to household sector</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Credit for housing purchases</td>
<td>10.0</td>
<td>5.0</td>
<td>5.9</td>
<td>7.3</td>
</tr>
<tr>
<td>Consumer credit</td>
<td>0.0</td>
<td>0.3</td>
<td>0.1</td>
<td>0.2</td>
</tr>
<tr>
<td>Other credit to households</td>
<td>4.2</td>
<td>13.5</td>
<td>13.0</td>
<td>12.1</td>
</tr>
<tr>
<td>Total credit portfolio of leasing companies</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
</tbody>
</table>

Source: Bank of Latvia

The leasing market is highly concentrated and the leading companies are bank subsidiaries. Around 60 percent of the leasing market is concentrated in two companies (Swedbank Līzings and SEB Līzings), which are subsidiaries of Swedish banks. The third leading company has a market share above 10 percent
and is also a bank subsidiary (DnB NORD Lizings). The top three companies lead the market in different types of products (e.g. financial leasing, operational leasing, factoring).\footnote{Information obtained from the website of the Latvian Lessors’ Association.}

**Leasing operations in Latvia are not regulated by a special law but governed by the Commercial Law and the Consumer Rights Protection Law.** However, as more than 90 percent of assets in the leasing sector are in companies that are either bank subsidiaries or linked with the banking sector, the leasing companies fall under scope of the Credit Institutions Law. This fact has two important consequences: (i) information about the consumer’s credit behavior is submitted to the Credit Register; and, (ii) some sort of supervision is exercised by the Financial and Capital Market Commission (FCMC), not from a business conduct but a prudential perspective.

**Credit Unions**

Despite continuous growth throughout the decade, the assets of credit unions represent a smaller share of financial sector assets in 2008 relative to 2001. Credit unions’ total assets have grown at an average annual rate of 28 percent for the past seven years, increasing from LVL 1.7 million in 2001 to LVL 9.3 million in 2008. However, this growth rate has been one of the lowest within the NBCI segment and the overall financial system (e.g. leasing companies grew around 40 percent and other NBCI grew around 56 percent). Thus, the share of credit unions’ assets within the NBCI segment decreased from 0.5 percent in 2001 to 0.3 percent in 2008.

**Consumer credit represents more than half of the loan portfolio of credit unions.** About 65 percent of the total lending by credit unions as of June 2009 corresponds to consumer credit, a slight decrease of 2.7 percentage points relative to December 2004. Still, consumer credits have grown 90 percent from December 2004 to June 2009, reaching a level of LVL 5.3 million. In the same period, mortgage loans have grown 106 percent and reached a level of LVL 2.6 million. As of June 2009, mortgage loans represent about 32 percent of the credit unions’ loan portfolio.

![Figure 8: Loan Portfolio Structure of Credit Unions](source: FCMC)

Almost half of the loan portfolio corresponds to medium-term loans, with a maturity of 1-5 years. Medium-term loans have increased their participation in the loan portfolio from 25 percent in December...
2004 to 46 percent in June 2009. On the contrary, short-term loans (maturity of less than 1 year) have decreased their share in the past 5 years, from 50 percent in December 2004 to 21 percent in June 2009.

![Figure 9: Maturity of Credit Unions’ Loan Portfolio (in percentage)](source)

The quality of the loan portfolio of credit unions deteriorated in 2008 but has slightly recovered in the first half of 2009. The share of standard loans in the total loan portfolio decreased from 75 percent in December 2007 to 69 percent in December 2008. The deterioration of the loan portfolio’s quality is explained by increases of 38 percent in close-watch loans and 66 percent in non-performing loans. During the first half of 2009, close-watch loans decreased 11 percent and non-performing loans fell 7 percent. Thus, their joint share within the loan portfolio decreased from 31 to 28 percent.

![Figure 10: Quality of Credit Unions’ Loan Portfolio (in percentage)](source)

**Legal Framework and Institutional Arrangements**

The main legislation governing consumer protection issues for non-bank credit institutions are:

- Consumer Rights Protection Law (March 1999, as last amended in June 2009).
- Credit Institutions Law (effective 1 January 2007, as last amended in February 2007)
- Cooperative Company Law
Latvia  Non-bank Credit Institutions Segment

- Regulation for the Credit Register, Bank of Latvia Regulation No. 32/2009
- Regulations Regarding Consumer Credit Arrangements, Cabinet Regulation No. 692 (25 August 2008)
- Advertising Law (January 2000, as last amended in December 2007)
- Personal Data Protection Law (April 2000, as last amended in 2006);
- Commercial Law
- Cabinet Regulations on Procedures for the Submission and examination of Consumer Claims Regarding the Non-conformity of Goods or Services with Contract Provisions, Cabinet Regulation No. 631 (1 August 2006)
- Regulations of the Council of FCMC on the Issue of Credit Institutions and Credit Union Operating Licences (2002)
- Regulations of the Council of FCMC on Obtaining Operation Permits by Credit Institutions and Credit Union Operating (December 2002)

The Consumer Rights Protection Center (CPC) has the responsibility of protecting consumers from unfair and deceptive business practices, including practices in the financial sector.

The Financial and Capital Market Commission (FCMC) is in charge of licensing and supervising the activities of credit unions

The Latvian Lessors’ Association was founded in October 2000 as the representative body for the leasing industry and it has adopted a code of ethics which includes a section on relations with customers.

The Latvian Cooperative Credit Union Association (LCCUA) represents Latvian cooperative financial organizations and international organizations for microcredit development, and is a self-regulatory organization for the industry. The association enforces a code of conduct for credit cooperatives.

**Key Recommendations**

The key recommendations from the review of consumer protection issues for non-bank credit institutions are the following:

- Develop specific legislation to regulate operations and supervise business conduct of leasing companies. Issue regulations for licensing NBCIs, other than credit unions, especially if involved in mortgage loans and mortgage-backed consumer loans.
- Corporations specialized in mortgage and consumer lending should engage in establishing an industry association that would represent and build consensus among its members. The associations should adopt codes of conduct with a specific section devoted to interactions with consumers, and be responsible for enforcing the adopted code of conduct among its members. The code of conduct should be visibly displayed in all points of sale or branches of the NBCIs and on the web sites of the associations and members.
- Loan officers in NBCIs should be trained. They should interview their customers to understand their financial situation and the risks they are facing, and provide them with instructions on how to maintain sound personal finance and avoid overexposure to risks. These practices for loan officers should be described in detail in the internal procedures of the NBCIs.
• There should be requirements on education, experience and integrity that loan officers and point-of-sale representatives are obliged to satisfy. These requirements should be formalized and agreed upon within the industry.

• NBCI associations should engage in initiatives that would increase disclosure of pre-contractual information to consumers (e.g. terms and conditions available in branches, points of sale and institutions’ websites) and enhance awareness and clarity of complaints procedures, both within NBCIs and for out-of-court dispute resolution mechanisms (e.g. inclusion of the channels available for complaints submission in the codes of conduct and general terms and conditions).

• The CRPC statutory power and technical capacity in the area of financial services should be strengthened. The CRPC should (i) arrange secondment of staff from the FCMC, (ii) develop twinning arrangements with partner institutions in the EU, (iii) plan and conduct on-site inspections for supervision on compliance with consumer protection legislation.

• More resources should be channeled to consumer associations and earmarked to their engagement in financial education. Consumer associations should be more heavily involved in product comparison, comparison of disclosure practices, sales practices, communication of principles of sound personal finance, etc.

• Provide resources and undertake financial literacy surveys for better targeting financial literacy programs and evaluating the efficiency and efficacy of such programs.
## Good Practices: Non-bank Credit Institutions Segment

<table>
<thead>
<tr>
<th>SECTION A</th>
<th>CONSUMER PROTECTION INSTITUTIONS</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Good Practice A.1</strong></td>
<td><strong>Consumer Protection Regime</strong></td>
</tr>
<tr>
<td>The law should provide for clear rules on consumer protection in the area of non-bank credit institutions, and there must be adequate institutional arrangements for implementation and enforcement of consumer protection rules.</td>
<td></td>
</tr>
<tr>
<td>a. There should be specific provisions in the law, which create an effective regime for the protection of consumers of non-bank credit institutions</td>
<td></td>
</tr>
<tr>
<td>b. The rules should prioritize a role for the private sector, including voluntary consumer protection organizations and self-regulatory organizations.</td>
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</tbody>
</table>

### Description

**a.** The Consumer Rights Protection Law applies equally to banks and non-bank credit institutions. Rules are also provided in respect of any financial product or service, whether or not provided by a regulated financial entity. The objective of the laws is “to ensure that consumers are able to exercise and protect their lawful rights when entering into contracts with goods and service providers.” The Unfair Commercial Practices Prohibition Law, the Advertising Law, as well as other regulations complete the legal framework for consumer protection in respect of financial services provided by NBCIs. These laws are implemented by the Consumer Rights Protection Centre (CRPC) that is subordinated to the Ministry of Economics, as a “direct administration institution”. The capacity of the CRPC to supervise NBCIs from the business conduct point of view is very limited and is done only in direct connection with specific complaints.

The non-bank credit sector comprises mainly leasing companies, credit unions and other financial intermediaries acting as credit providers. The frameworks for their establishment, licensing and supervision from the business conduct point of views varies, as follows:

- The establishment of **leasing companies** and **credit providers** is governed by the provisions on joint stock companies and limited liability companies under the *Commercial Law*.
- The establishment of the **credit unions** is governed by the Credit Union Law, and the Cooperative Company Law.
- Leasing companies do not have a special law to govern their operations and supervision. Only the leasing companies established as banks subsidiaries or linked to the banks are indirectly supervised by FCMC, in line with the provisions of the Credit Institutions Law. In Latvia 13 out of the 23 leasing companies are banks’ subsidiaries and represent about 95 percent of the leasing companies. Therefore they are subject to limited supervision by the FCMC, from a prudential supervision perspective only. The remaining companies are not supervised.
- Credit unions are licensed and receive permit for operations by FCMC. They are participants to the Credit Register (public credit register administered by the Bank of Latvia). In Latvia 35 credit unions have license and permit to operate.
- Financial institutions that provide mortgage and consumer loans but do not fall under the legal definition of credit institutions are neither supervised nor regulated. However, they are obliged to follow the provisions set out by the Consumer Rights Protection Law and the Personal Data Protection Law.

**b.** The Consumer Rights Protection Law provides consumer associations with a clear role in consumer rights protection. Thus associations have the right to: (i) participate, together with supervisory and control institutions for consumer rights in inspections related to quality compliance of goods and services delivered; (ii) examine complaints and proposals from consumers and provide assistance when consumer rights have been violated; and (iii)
submit statements of claim to courts in respect to protection of consumer rights and represent the consumer’s interest in court.

In Latvia there is only one professional association in the NBCI segment, the Latvian Lessors’ Association, representing the thirteen leasing companies, subsidiaries of the banking sector.

**Recommendation**

Although there is no Leasing Directive at the EU level, specific legislation may be necessary to regulate operations supervise business conduct of leasing companies. Also some sort of licensing is necessary for NBCIs, other than credit unions, especially if involved in mortgage loans and mortgage-backed consumer loans.

**Good Practice A.2**

**Code of Conduct (Customer Protection Code)**

- There should be a principles-based Code of Conduct for non-bank credit institutions that is devised in consultation with the industries involved, and is monitored and enforced in the last resort by a statutory agency.
- The statutory Code should be limited to good business conduct principles. It should be augmented by voluntary codes on matters specific to the industry (banks, credit unions, other non-bank credit institutions).
- The operation of voluntary codes should be monitored by a statutory agency, and the Annual Report of that agency should comment on the operation of those codes.

**Description**

The Latvian Lessors’ Association has developed a code of conduct to which all the thirteen members have adhered. However, this code of conduct is posted neither on the Association’s website, nor on each individual company’s sites.

The Latvian Cooperative Credit Unions Association (LCCUA) is a self-regulated association. However, its presence in the financial sector is not very visible.

No association is established by other companies specialized in mortgage and consumer lending.

**Recommendation**

Corporations specialized in mortgage and consumer lending should engage in forming an industry association which would represent and build consensus among its members. The process of building consensus and harmonizing practices in the industry should include the adoption of a code of conduct with a specific section devoted to interactions with consumers. The newly formed association should be also responsible for enforcement of the adopted code of ethics among its members.

The Latvian Lessors’ Association should explicitly engage in enforcement of the adopted code of conduct within its members. It should report regularly on breaches of the code of conduct by their members and non-members within the scope of the code of conduct.

LCCUA needs to provide greater awareness and visibility of consumers’ rights and improve the commitment for fair lending practices by the adoption and observance of a code of conduct. It should report regularly on breaches of the code of conduct by their members and non-members within the scope of the code of conduct.

**Good Practice A.3**

**Other Institutional Arrangements**

- There should be an equal balance between prudential supervision and consumer protection.
- The judicial system must provide credibility to the enforcement of the rules on financial consumer protection.
- The media and consumer associations ought to play an active role in promoting financial consumer protection.
- Non-bank credit institutions should be legally responsible for all statements made in marketing and sales materials related to their products.

**Description**

Prudential supervision is conducted over credit unions and in a more limited extent over leasing companies, but only those established as bank subsidiaries. Credit unions and
leasing companies that are banks subsidiaries report financial information to the FCMC. The Bank of Latvia receives some financial information about other NBCIs from the Central Bureau of Statistics for the annual Financial Stability Report. However, there is a limited amount of knowledge regarding the size and problems encountered by these institutions.

Consumer protection monitoring and supervision of NBCIs is conducted by the CRPC and is based on complaints from consumers under the Consumer Rights Protection Law.

b. In relation to the products of the NBCIs, consumers are aware of their rights in a limited extent; the appropriate authority to file complaints with is the CRPC—for complaints unresolved to their satisfaction at the individual NBCI level. CRPC is entitled to issue binding corrective orders, administrative acts or to impose fines.

c. The consumer protection associations, the press and media are becoming active in the area of financial consumer protection, especially by mirroring the initiatives at the EU level. However, given their very limited resources, their activity is far from being satisfactory and even the sustainability of such associations is put under question mark.

d. The CRPC is responsible for monitoring and investigating cases of misleading and unfair advertising. However, their activity is rather reactive, based on complaints from consumers and firms (competitors). No systematic supervision form is undertaken. While market participants point to occasional cases of misleading advertising, the complaints in the area of NBCI are mostly initiated by consumers rather than competitors.

**Recommendation**

Greater awareness of consumer rights in all three areas of NBCI could be ensured by establishing stronger links between NBCIs, professional associations and consumer protection associations. However a prerequisite would be the strengthening of capacities of all such institutions by provisioning adequate resources.

To educate their consumers, NBCI associations should engage in initiatives that would increase disclosure of pre-contractual information to consumers (e.g. through regular product comparison of NBCIs in the press) and require the disclosure of clear complaints procedures within NBCIs themselves and with the CRPC and the court, and disclosure of all the available channels for submission of complaints in the codes of conduct and the general contracts’ terms and condition of NBCIs.

<table>
<thead>
<tr>
<th>SECTION B</th>
<th>DISCLOSURE AND SALES PRACTICES</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Good Practice B.1</strong></td>
<td><strong>Know Your Customer</strong></td>
</tr>
<tr>
<td></td>
<td>A non-bank credit institution must gather, file or record sufficient information appropriate to the risk of the transaction, the nature and complexity of the product or service being sought by the consumer.</td>
</tr>
<tr>
<td></td>
<td><strong>Affordability</strong></td>
</tr>
<tr>
<td></td>
<td>A non-bank credit institution must ensure that, under consideration of information disclosed by the consumer or third parties, any product or service offered to a consumer is adequately based upon possible affordability of the consumer.</td>
</tr>
<tr>
<td><strong>Description</strong></td>
<td>Reportedly, NBCIs collect information of their customers to screen their creditworthiness. NBCIs keep a file of each customer in line with the Data State Inspectorate regulations and, upon request, the customer is allowed to view the information stored. Since most of the NBCIs (with the exception of the thirteen leasing companies and the credit unions) are not participants of the public Credit Register, the customer risk assessment is done mainly based on the information held in their private register, which contains only negative information. The diversity of products and terms is more limited in case of NBCIs and their variation comes primarily from the choice of maturity. In this context NBCIs do not appear to advise customers on a sound ratio of debt service charges to income. NBCIs also often receive requests from customers to extend the maturity of their existing loan, which the</td>
</tr>
</tbody>
</table>
NBCIs reportedly do without a rescheduling fee but at a higher interest rate -- assuming an upward sloping yield curve.

**Recommendation**

The loan officers of the NBCI should be trained in, and provide the consumer with, instructions on how to maintain sound personal finance. They should conduct interviews to understand the personal/household balance sheet composition and the risks their customer is facing to avoid overexposure of the consumer to changes in interest rates and to avoid endangering his or her credit history and future ability to borrow. They should also advise the client to access their credit history from the Credit Register. These practices should be described in detail in the internal procedures of the NBCI, and the principles and the entitlements of consumers to such treatment and service should be included in the code of conduct of the industry, to be displayed visibly in each point of sale or NBCI branch.

The general terms and conditions of the NBCIs’ contracts should be available to consumers upon request in NBCIs branches and points of sale, and readily available for download from their respective websites.

The requirements on education, experience or integrity that the loan officers and points of sale representatives are obliged to satisfy should be formalized and agreed upon within the industry associations.

**Good Practice B.2**  

*Cooling-off Period*

Unless explicitly waived by the consumer in writing there should be a cooling-off period of fourteen days associated with all credit products.

**Description**

The Consumer Rights Protection Law provides that the consumer has the right "to withdraw unilaterally from a contract within a specified time period without payment of penalties, interest or compensation for losses." However this right may be exercised only in the event that: (i) the contract was entered into outside the permanent location of provision of services; (ii) the contract is a distance contract; (iii) the contract involved obtaining the right of temporary occupancy of the whole or part of a residential building. In these instances, at the time the contract takes effect, the service provider is obliged to submit to the consumer a written withdrawal form indicating the name and address of the service provider, as well as a description of the right of withdrawal. In the case of a credit institution, by sending the withdrawal within a specified time period, the contract is terminated and the consumer released from any contractual obligations. While it is the duty of the consumer to return "goods" within thirteen days following the date the consumer sends the completed written withdrawal form, it is unclear what the "specific time" is to return funds received from a service provider.

**Recommendation**

It is recommended that loans to consumers be subject to a cooling-off period of 14 days. The EU directive on consumer credit makes mandatory this provision. The Directive needs to be enforced through national legislation by March 2010.

**Good Practice B.3**  

*Bundling and Tying Clauses*

Whenever a non-bank credit institution contracts with another merchant to distribute its credit contracts, no product should be offered “only” in a bundle without being available separately,

**Description**

Market participants report that tying of financial services could take place on occasions, particularly in mortgage loans or mortgage backed loans.

**Recommendation**

NBCIs should clearly provide customers with separate prices of each product in a bundle, as well as any discount available if purchased as a bundle from the same NBCI (or from an NBCI’s preferred vendor). The code of conduct of NBCIs should include these requirements and state that compulsory tying of financial products or their availability exclusively in bundles are prohibited sales practices.

**Good Practice B.4**  

*General Practices*

Customer disclosure and sales practices should be included in the non-bank credit institutions’ code of conduct and monitored by the supervisory authority.
Description

There is no requirement for a harmonized, simple fact sheet to be provided to customers to facilitate comparability of similar products’ conditions, especially costs, risks and contractual obligations. Sales practices are described in internal rules for loan/sales officers and their consistency with the principles of sales to consumers in the code of conduct is reportedly ensured in the case of leasing companies. Due to the fact that the NBCIs are not subject to prudential or business conduct supervision, the monitoring and enforcement of the code of conduct is effectively left to the NBCIs’ associations. Only the Latvian Lessors’ Association reports that brochures and leaflets are provided to customers with simple but material information on products’ characteristics.

Recommendation

See recommendation A.2.

Good Practice B.5

Roles of Third Parties

a. The regulator or supervisor ought to publish annual public reports on the development, health, strength and penetration of the non-bank credit institutions either as a special report or as part of the disclosure and accountability requirements under the law governing it.
b. Non-bank credit institutions should be required to provide their financial information to enable the general public to form an opinion as to the financial viability of the institution.

Description

The FCMC requires credit unions to report financial accounting information and statistics. The FCMC publishes aggregated financial information of credit unions as well as an analysis of the loan portfolio of the sector.

The Bank of Latvia publishes aggregate financial statements and statistics of the leasing companies, obtained from the Central Statistical Bureau. The Bank of Latvia includes data of leasing companies, credit unions and other NBCIs in the Financial Stability Report.

The other NBCIs are required to prepare annual reports for their shareholders. However these annual reports are not commonly disclosed to customers nor are the customers sufficiently aware of their right to view the reports.

Recommendation

The annual reports of NBCIs should be available in NBCIs’ branches to customers upon request and published on the NBCIs websites.

SECTION C

PRIVACY AND DATA PROTECTION

Good Practice C.1

Non-bank credit institutions’ customers have a right to expect that their financial transactions are kept confidential. The law ought to require non-bank credit institutions to ensure that they protect the confidentiality and security of personal data, against any anticipated threats or hazards to the security or integrity of such information, and against unauthorized access.

Description

The Personal Data Protection Law requires NBCIs to be registered as personal data system administrators and strictly obey the rules specified in the Law.

Recommendation

Consumers’ awareness of their right to view the personal file that an NBCI keeps on them should be raised by including this right in the code of conduct. Consumers’ awareness of the fact that incorrect or incomplete information in their file can impede their ability to borrow in the future should be increased by consumer protection associations, NBCIs associations and the media.

Good Practice C.2

Credit Bureaus

a. A non-bank credit institution must ensure the accuracy and timeliness of the information that it shares.
b. Credit bureaus must comply with the timeliness of updating information of consumers.
c. Customers’ records should be kept confidential and only be provided for permitted and lawful purposes.
d. There ought to be clear procedures and rules on the retention period of credit records, and customers must be informed about the retention
### Description

The Credit Register operated by the Bank of Latvia is the only industry-wide credit register in Latvia. The Register collects positive and negative information from banks, bank subsidiaries engaged in credit activities, insurance companies and credit unions. About four debt collection companies and several NBCIs store data about their clients' credit history and act as *de facto* credit bureaus, but their information is not accounted in any official statistics.

**a.** The Credit Institutions Law (Article 106) provides that all banks, as well as their subsidiaries, are required to submit information to the Bank of Latvia regarding the debtors and the course of fulfillment of their commitments. This provision applies by default to leasing companies that are linked to banking sector and to credit unions. The Law is silent on the duty of a bank or its subsidiary to obtain the customer’s consent or inform the customer that it will submit such information. However, the Personal Data Protection Law (Section 7), applicable to NBCIs, states that personal data processing is permitted only if, among other conditions, at least one of the following is met: i) consumers give his or her consent for personal data processing, ii) such personal data processing results from contractual obligations or, taking into account a request from the consumer, the processing of data is necessary in order to enter into a relevant contract. The consent should be a freely, unmistakably expressed affirmation of the wishes of a data subject, by which the data subject allows his or her personal data to be processed.

**b.** According to the Regulation 32 of the Bank of Latvia, any person has the right to verify the information relating to him in the Credit Register, including the names of the banks and their subsidiary financial institutions which have submitted the information to the Credit Register. Upon a legitimate request from a customer, the Bank of Latvia provides the requested information within five working days. If a person considers that the information in the Credit Register is incorrect, he or she may request that the information be adjusted or updated by the credit institution which submitted it to the Register. No longer than one working day (Article 21) from receipt of the request, the institution in question must send an instruction to the Credit Register to make the necessary adjustments. Similarly, after private credit bureaus provide a person with his credit report, the person must take up any disputes with the institution that provided the information to the system administrators that are acting as private credit bureau. The credit bureau will change information only if instructed by the institution that provided the information.

**c.** In accordance with Regulations 32 and 34 of the Bank of Latvia, the Credit Register shall provide participant credit institutions with information on the credit history of particular customers against the payment of a fee. Articles 38-40 of Regulation 32 provide that Credit Register’s participants are entitled to receive the information collected on the Credit Register’s database in a manner which does not directly or indirectly identify a borrower or borrower’s guarantor, neither the participants that submitted information in the Register. The FCMC has also the right to receive aggregated information of the Credit Register in a manner which does not directly or indirectly identify a borrower or borrower's guarantor. The Credit Register can provide information only to the participant credit institutions. Private credit bureaus may release data to other credit institutions only based on a prior consent from the customer as per the Personal Data Protection Law. The Credit Institutions Law states that credit institutions have the duty to guarantee the confidentiality of the identity, accounts, deposits and transactions of their customers. Such information can only be disclosed under specific circumstances (enumerated in Article 63)to state institutions, state officials or other institutions and officials. Intentional or non-intentional disclosure of such information falls under criminal procedure and applies equally to current and former employees of the credit institution, FCMC, Bank of Latvia or any other state institution or official that had access to such information.
### SECTION D  
**DISPUTE RESOLUTION MECHANISMS**

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#### Good Practice D.1  
**Complaint Handling**

Complaint resolution should be included in the non-bank credit institutions’ code and monitored by the supervisory authority.

**Description**

Complaints handling and resolution is not included in the leasing association’s code of conduct. The other NBCIs do not have a code of conduct. The NBCI sector is not supervised let alone their handling of complaints.

**Recommendation**

Complaints handling and resolution should be described in the NBCIs associations’ code of conduct, and reference to this description should be made in the general contract terms of the NBCIs. The market conduct of NBCIs should be supervised so that their operations and interactions with consumers are in line with the code of conduct adopted or required to be adopted by the industry.

#### Good Practice D.2  
**Formal Dispute Settlement Mechanisms**

- **a.** A system should be in place that allows consumers to seek affordable and efficient third-party recourse in the event they cannot resolve an issue with the non-bank credit institution, which could be an ombudsman or tribunal.

- **b.** The role of an ombudsman or equivalent institution *vis-à-vis* consumer complaints must be in place and made known to the public.
**c.** Ombudsman’s impartiality and independence from the appointing authority and industry must also be assured.

**d.** The enforcement mechanism of the decisions of the ombudsman or equivalent institution and binding nature of the decision on non-bank credit institutions must be in place and publicized.

| Description | a. Currently, the consumer has the choice of submitting a complaint, which is unresolved at the individual NBCI level, to the CRPC or to the FCMC (in the case of credit unions and leasing companies linked to banking sector) or both. In practice FCMC redirects the complaints to CRPC.  

b. There is no ombudsman for NBCIs in Latvia and the CRPC is the main statutory consumer protection advocate in the field of financial services provided by NBCIs. |

| Recommendation | There should be a clear institutional structure to deal with consumer complaints. A long-term option is establishing a financial ombudsman or a specialized financial consumer protection agency, but in the interim the authority and capacity of the CRPC should be expanded. The CRPC could set up a specialized unit, or at a minimum, hire specialized staff with expertise in financial services. Another option would be for the FCMC to play an increased role in financial consumer protection and the CRPC to be responsible of handling all financial consumers’ complaints and disputes. |

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**SECTION F  CONSUMER ADVOCACY AND FINANCIAL LITERACY**

**Good Practice F.1  Information Resources for Consumers of Financial Services**

a. Policymakers, industry and advocates should understand the financial capability of various market segments, particularly those most vulnerable to abuse.

b. Consumers, especially the most vulnerable, should have access to sufficient resources to enable them to understand financial products and services available to them.

| Description | There is consensus among policymakers, consumer advocates and industry about the need for consumers’ education in the area of financial services. The access of consumers to financial education is rather low at present, and so are the resources devoted to consumer protection associations to help out in this respect. However, the Ministry of Economics is engaged with the task of financial education following the EU wide program in this area.  

Not sufficient resources are available to vulnerable persons, especially if they are not digitally literate. Most of the public is currently being educated mainly through financial information disclosure, by shopping around for best deals and comparing products, through learning by doing, and bitter experiences of the on-going financial turmoil. |

| Recommendation | More resources should be channeled to consumer associations and earmarked for their engagement in financial education, product comparison, comparison of disclosure practices, sales practices, communication of principles of sound personal finance, etc.  

A financial literacy survey would be necessary to better identify the needs and to target interventions. The survey should be repeated every several years to assess the effectiveness of implemented financial education programs and measures to improve consumer protection. |
Latvia: Consumer Protection in the Securities Sector

Overview

Historically, consumer protection in securities area has developed somewhat differently than in banking. Bank customers in most countries enjoy deposit protection and strong prudential supervision of banks – factors that create a solid safety net for the customers. On the other hand, investors in securities are not guaranteed any returns, and hence, on average, are usually more sophisticated and financially educated than average bank customers. The most important market conduct regulations protecting the investors are those dealing with disclosure of a variety of investment information by industry intermediaries.

The NASDAQ OMX Riga stock exchange is part of the NASDAQ OMX Group. NASDAQ OMX Riga is a small stock exchange with only 35 listed shares, of which only 5 are on the First List of the exchange. The total market capitalization of NASDAQ OMX Riga as of the end of June 2009 was 1.0136 Billion EUR. The Riga Stock Exchange was founded in 1993 and its official opening took place in July 1995. The exchange was comprised of shares that had been privatized through the privatization process in the early 1990s. A number of major Latvian companies, particularly major utilities, has not been publicly privatized and listed on the exchange which, according to many commentators, has been the cause of the small size of the exchange.

Table 6: Market Capitalization of NASDAQ OMX Riga Exchange

<table>
<thead>
<tr>
<th></th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of Companies</td>
<td>39</td>
<td>45</td>
<td>40</td>
<td>41</td>
<td>38</td>
</tr>
<tr>
<td>Number of IPOs</td>
<td>1</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Market Capitalization</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>In EUR millions</td>
<td>1,207</td>
<td>2,122</td>
<td>2,034</td>
<td>2,098</td>
<td>1,829</td>
</tr>
<tr>
<td>As percent of GDP</td>
<td>10.8</td>
<td>16.5</td>
<td>12.6</td>
<td>10.5</td>
<td>7.7</td>
</tr>
<tr>
<td>Average Market Capitalization</td>
<td>30.9</td>
<td>47.2</td>
<td>50.9</td>
<td>51.2</td>
<td>48.1</td>
</tr>
</tbody>
</table>


The market participants are dominated by the subsidiaries of foreign banks, mostly from Scandinavian countries. Banks are structured as universal banks and most securities-related activities, such as investment fund sales, are done out of the branch offices, except for securities trading on NASDAQ OMX Riga. These securities trading activities must be done through an exchange-registered broker who is usually located in the home office. Under Article 112 of the Law on Financial Markets Instruments, a broker located in a member state of the EU does not have to be registered with the FCMC to sell foreign shares, if the regulatory authority in the member state provides FCMC with a statement including information required under Article 112.. The banks take the position that all sales in the branch offices are passive and based on approved sales literature available in the offices. There are very few independent securities brokers and their market share is quite small.
Table 7: Number and Size of Financial Brokerage Companies

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Banks</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Number of Banks</td>
<td>n.a.</td>
<td>20</td>
<td>20</td>
<td>n.a.</td>
</tr>
<tr>
<td>Assets of Resident Clients (LVL million)</td>
<td>849.1</td>
<td>929.3</td>
<td>1,166.4</td>
<td>n.a.</td>
</tr>
<tr>
<td><strong>Non-Banks</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Number of Brokers</td>
<td>5</td>
<td>6</td>
<td>6</td>
<td>8</td>
</tr>
<tr>
<td>Assets of Resident Clients (LVL million)</td>
<td>18.9</td>
<td>25.2</td>
<td>24.4</td>
<td>0.2</td>
</tr>
</tbody>
</table>

Source: FCMC, Quarterly Bulletins

Asset management companies are the most active entities in the securities markets due to the implementation of Pillar II of the pension program. Their pension plans are also available in the branch offices of banks and participants in the program can choose the plan they want and change the plan once a year. Banks express that there is no pressure on participants to change or enroll in plans from the employees of the branch offices.

Table 8: Number and Size of Asset Management Companies and Funds Managed

<table>
<thead>
<tr>
<th></th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of Asset Management Companies</td>
<td>10</td>
<td>10</td>
<td>13</td>
<td>14</td>
<td>15</td>
</tr>
<tr>
<td>Number of Investment Funds</td>
<td>15</td>
<td>17</td>
<td>20</td>
<td>34</td>
<td>38</td>
</tr>
<tr>
<td>Open-End</td>
<td>11</td>
<td>13</td>
<td>15</td>
<td>27</td>
<td>28</td>
</tr>
<tr>
<td>Sub-Funds</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>10</td>
<td>10</td>
</tr>
<tr>
<td>Closed-End</td>
<td>4</td>
<td>4</td>
<td>5</td>
<td>7</td>
<td>10</td>
</tr>
<tr>
<td>Number of investment certificates</td>
<td>6,743,151</td>
<td>25,336,985</td>
<td>38,501,189</td>
<td>46,429,990</td>
<td>63,207,065</td>
</tr>
<tr>
<td>Number of Pillar II investment plans</td>
<td>18</td>
<td>22</td>
<td>25</td>
<td>25</td>
<td>27</td>
</tr>
<tr>
<td>Number of participants in Pillar II plans</td>
<td>633,685</td>
<td>900,098</td>
<td>900,098</td>
<td>997,684</td>
<td>1,065,564</td>
</tr>
</tbody>
</table>

Source: FCMC, Quarterly Bulletins

Nonetheless, even for the asset management companies, there has been a sharp decline in business as a result of the financial crisis in Latvia. After reaching a peak level of LVL 248 million by June 2008, the total assets of investment funds declined sharply in the last half of 2008, especially from September to December (44 percent). In the first quarter of 2009, the level of investment fund assets slightly recovered, increasing about 12 percent.

Figure 11: Investment Fund Assets
(in LVL millions)

Source: FCMC, Quarterly Bulletins
As a result of the purchase of the Riga Stock Exchange by the NASDAQ OMX Group, the technical framework for the market in terms of exchange operations is excellent and meets with high international standards. The shares are organized as part of a Baltic List of companies on the NASDAQ OMX software and websites, as a method of increasing interest and liquidity. However the Baltic shares of Lithuania, Latvia and Estonia are separated from the Nordic List of companies covering the Scandinavian markets (Denmark, Sweden, Finland and Iceland).

The aggregation of the shares in the Baltic List has not gone hand in hand with consolidated regulation. The regulation of the securities markets of each of the Baltic countries is still conducted on a national level, including registration requirements, supervision of intermediaries and funds, and enforcement of legal requirements. As a result, the costs and benefits of an integrated market have not yet been fully realized in Latvia or the other Baltic countries.

The Latvian government created a consolidated regulator in 2001, the Financial and Capital Market Commission (FCMC), which regulates the securities, banking, insurance and private pension sectors. The regulation of the securities markets changed markedly with the adoption of the Law on Financial Market Instruments in 2004. This law transposed the EU MiFID Directive into Latvian law. The Latvian regulatory system can be characterized as a principles-based regulatory system very similar to the Swedish model. Regulation of the market participants is primarily left up to the internal rules of the participants. The FCMC conducts on-site inspections from time to time to verify the operation of the market participants in compliance with the general rules of the FCMC and the Law on Financial Market Instruments.

There have been unregistered securities and foreign currency cash and derivatives ("forex") sales activities by entities that are not regulated by the FCMC. There have been several complaints that these are Ponzi schemes that do not invest the money as promised by the promoters. The current regulator structure does not appear to cover these entities and as a result it is difficult to determine the extent of these schemes but it appears that they drain a significant amount of capital from retail investors that could be used in the regulated markets. In addition, they create a lack of trust on the part of investors in any investment activity. It is worth to note that in cases where FCMC possess information on unlicensed activities in securities area, the FCMC issues a warning to the public and sends the information to the Police to start criminal proceeding.

Retail investors in the regulated markets in Latvia are primarily involved in the securities markets through the Pillar II pension funds. This is the result of the mandatory character of the Pillar II funds and the lack of investment products on the NASDAQ OMX Riga exchange. It could also be attributable to a lack of investor education and literacy, two programs that are not actively pursued in Latvia. In addition, the lack of new IPOs, through privatization or otherwise, has meant that the investing public has not received the practical education in the securities markets that is a side product of large IPOs and has furthered investor education and awareness in other Eastern European countries.

The corporate financing in Latvia in the past decade has shown a clear preference for bank funds over market financing for the capital needs of corporations and other businesses. The result has been an underdeveloped stock market with limited investment products. However, the use of banks for corporate finance may be reduced to a certain extent as a result of the recent financial crisis, as corporations look for additional avenues of financing. This could provide a wider range of financial products and more opportunity for retail investors in Latvia.
Legal Framework and Institutional Arrangement

The following are the key laws and regulations addressing consumer protection in the securities sector:

- Law on Financial Markets Instruments (LFMI);
- Law on Investment Management Companies;
- Investor Protection Law;
- Consumer Rights Protection Law;
- Advertising Law;
- Personal Data Protection Law;
- Unfair Commercial Practices Prohibition Law;
- Regulations on the Requirements to be Complied with When Presenting Investment Recommendations;
- Regulations regarding Distance Contracts for the Provision of Financial Services;
- Regulation for the Completion and Keeping of Source Documents Associated with Financial Instrument Transactions;
- Recommendations for Keeping Records of Publicly Traded Financial Instruments Not Registered with the Latvian Central Depository;
- Regulations on information that, when providing investment services, should be given to customers regarding investment services, financial instruments, charges and performed transactions (available in Latvian)

The Financial and Capital Market Commission (FCMC) is a consolidated regulator that has the responsibility for supervising the banking, insurance and securities sectors of the financial markets. The FCMC acts primarily as a prudential regulator, although it engages in some market conduct regulation as well.

NASDAQ OMX Riga is part of the Baltic Market of NASDAQ OMX. It shares the same trading platform as other exchanges in the NASDAQ OMX Group, including the other members of the Baltic Market, Lithuania and Estonia. The Riga exchange is still regulated under domestic Latvian legislation by the FCMC, notwithstanding that is part of an international group of exchanges.

The Latvian Central Depository was purchased by the Riga Stock Exchange in 2002 and is now owned and operated by NASDAQ OMX Riga.

The Consumer Rights Protection Centre (CRPC) is a direct administration institution supervised by the Ministry of Economics. It has dual responsibility with the FCMC for the protection of investors in the securities markets and co-ordinates with the FCMC in handling complaints from investors.

There are two main professional associations in the securities markets, the Securities Committee of the Association of Latvian Commercial Banks and the Latvian Association of Professional Participants in Financial Markets. These associations act on behalf of their members in commenting on, and helping to prepare, legislation related to the securities market. However, their activity does not extend beyond the advocacy of their professional members. They do not engage in consumer education or dispute resolution.
The **Data Protection Inspectorate** has the responsibility for enforcing the Personal Data Protection Law and has dual responsibility with the FCMC for enforcing the Law as to securities markets participants.

**Key Recommendations**

- An MOU between FCMC and CRPC would help to clearly define their relationship, jurisdiction and responsibilities regarding the securities market.
- A code of conduct for salespeople of securities and CIU units would be useful in the current environment to restore trust among retail investors.
- The sanctions regime for the FCMC and CRPC should be enhanced to make them more effective.
- The marketing rules should be the same for all manner of sales activities (distance or direct sales) to avoid any kind of regulatory arbitrage. Attention should be paid to marketing rules included in different regulations such as LFMI, Investor Protection Law and FCMC Regulations.
- Individuals dealing with customers regarding securities, investment funds and private pension funds should be examined and licensed.
- The penalties for improper sales practices are weak and should be significantly strengthened.
- Regulation should provide that electronic statements be sent in an easy-to-read and readily understandable format.
- An alternative dispute resolution mechanism is needed in order to handle financial disputes, and especially to fast track small claims.
- The FCMC should initiate and implement a program of investor education in conjunction with NASDAQ OMX Riga.
# Good Practices: Securities Sector

## SECTION A

### INVESTOR PROTECTION INSTITUTIONS

#### Good Practice A.1

**Consumer Protection Regime**

The law should provide for clear rules on investor protection in the area of securities markets products and services, and there should be adequate institutional arrangements for implementation and enforcement of investor protection rules.

- a. There should be specific legal provisions in the law, which create an effective regime for the protection of investors in securities.
- b. There should be a governmental agency responsible for data collection and analysis (including complaints, disputes and inquiries) and for the oversight and enforcement of investor protection laws and regulations.

#### Description

a. Latvian law contains numerous legal provisions for the protection of investors in securities. The Law on the Financial and Capital Market Commission created the FCMC as the consolidated regulator that is charged, as one of its responsibilities, with protecting investors in securities. In 2004, Latvia transposed the MiFID Directive into Latvian law in the Law on Financial Markets Instruments (LFMI) that contains extensive investor protection provisions. In addition, the Law on Investment Management Companies provides for specific protection for investors in investment funds. Finally, the Consumer Rights Protection Law and related laws, such as the Advertising Law and the Unfair Commercial Practices Prohibition Law also contain consumer protection provisions that are applicable to securities.

b. In addition to the FCMC, the Consumer Rights Protection Center (CRPC) is also responsible for handling customer complaints. Article 128 (14) and (15) of LFMI states that investors as consumers can complain to the CRPC regarding securities transactions. In practice, the CRPC will refer these complaints to the Securities Department of the FCMC for their handling. The FCMC also handles investor complaints that come directly to it. Section 26 of the Consumer Rights Protection Law also gives dual jurisdiction over investor complaints to FCMC and CRPC. The CPRC appears to be the agency that keeps the data for consumer complaints.

Overall the legal structure for investor protection is broad. However, neither FCMC nor CPRC have extensive enforcement powers. They have the right to levy fines, up to a maximum of LVL 10,000 (around USD 20,000), and to revoke licenses, but the law gives them little else in the way of sanctions. The power of both entities rests with their relationships with regulated entities to require compliance with the laws and regulations.

#### Recommendation

In cases of dual jurisdiction, matters can fall between the activities of the two agencies because one party thinks the other is handling the matter. Many jurisdictions have found that a MOU between the two agencies helps to clearly define their relationship, jurisdiction and responsibilities. This would probably be helpful in Latvia and FCMC and CRPC should consider entering into such an MOU.

In addition, the sanctions regime for FCMC and CRPC should be enhanced to make them more effective.

#### Good Practice A.2

**Code of Conduct for Securities Intermediaries and Collective Investment Undertakings.**

- a. Securities Intermediaries and CIUs should have a voluntary code of conduct.
- b. Securities Intermediaries and CIUs should publicize the code of conduct.
a. There is an industry Code of Conduct developed by the Latvian Association of Professional Participants in Financial Markets but it is very general in character and has not been used after the passage of LFMI. Under LFMI each financial institution should develop its own rules for conflicts of interest (Article 126), personal transactions (Articles 127-1 and 127-2) and dealings with other persons (Article 128). These are done with the approval of the FCMC.

Interestingly, Section 5 of the Unfair Commercial Practices Prohibition Law provides that "the performers of economic or professional activity or professional associations established thereof may develop a good practice code," which is a "voluntary agreement of the performers of an economic or a professional activity or an aggregate of provisions, which is not regulated in the regulatory enactments and shall regulate the behavior of such performers of commercial practices." The securities industry has taken the position that the LFMI has regulated consumer protection and therefore the Code is not necessary. However, there is no standardized Code that is applicable across the securities industry, with each investment brokerage firm creating its own rules to meet the FCMC's requirements.

b. There does not appear to be any publication of the conduct rules by the credit institutions and investment brokerage firms.

c. Since there is no industry-wide Code, this element is moot.

Recommendation

Although there is a general obligation for each investment firm to create an internal conduct regulation in order to meet the set of consumer protection principles in the LFMI, there is no standard industry-wide code of conduct. To increase investor trust, such a Code would be useful in the current environment, particularly if it is published, and should be considered by the securities industry.

Good Practice A.3 Other Institutional Arrangements

a. The judicial system should provide an efficient and trusted venue for the enforcement of laws and regulations on investor protection.

b. The media should play an active role in promoting investor protection.

c. The private sector, including voluntary investor protection organizations, industry associations and, where permitted, self-regulatory organizations should play an active role in promoting investor protection.

Description

a. The courts appear to be the most trusted venue for resolving securities investor's disputes.

b. Private TV shows and the financial news appear to cover the financial sector extensively.

c. There is a surprising lack of industry associations and NGO activity in the securities sector. This is probably due to the small size of the sector. In fact, NASDAQ-OMX Riga does most of the consumer protection promotion in the private sector through its website and the promotional campaigns for the exchange.

Recommendation

Increased NGO involvement should be encouraged but will probably not take hold until the securities sector recovers and more stocks are listed on the exchange.

SECTION B DISCLOSURE AND SALES PRACTICES

Good Practice B.1 General Practices

There should be disclosure principles that cover an investor's relationship with a
person buying or selling securities, or offering to do so, in all three stages of such relationship: pre-sale, point of sale, and post-sale.

a. The information available and provided to an investor should inform the investor of the choice of accounts, products and services; the characteristics of each type of account, product or service; and the risks and consequences of purchasing each type of account, product or service.

b. A securities intermediary or CIU should be legally responsible for all statements made in marketing and sales materials related to its products.

c. A natural person acting as the representative of a securities intermediary or CIU should disclose to an investor whether he is licensed to act as such a representative and by whom he is licensed.

| Description | a. Articles 128(6)(1)&(2) and (7) of LFMI require that investors be informed as to product services and characteristics by an investment brokerage firm. This information includes:
1) the investment brokerage firm or the credit institution and the investment services and ancillary (non-core) investment services it provides;
2) financial instruments and investment strategies offered, risks associated with investments in respective financial instruments or with a particular investment strategy;
3) execution venues;
4) costs of offered services and associated charges.

b. Section 10 of the Advertising Law provides that advertisers shall be liable for the content of their advertising. Consequently, the securities investment firms are responsible for their marketing.

c. Article 126-1 of LFMI provides that an investment brokerage firm must identify itself to potential customers and Article 6 of the Regulation regarding Distance Contracts for the Provision of Financial Services provides that the identity of service provider and any licenses required to give the service must be disclosed. In addition, Article 12 of the Regulation provides that if an investor is contacted by telephone, the caller must identify himself or herself and state his or her relation with the service provider (i.e. investment brokerage firm). |

| Recommendation | No recommendation. |

| Good Practice B.2 | Terms and Conditions |

Before commencing a relationship with an investor, a securities intermediary or CIU should provide the investor with a copy of its general terms and conditions, and any terms and conditions that apply to the particular account.

Insofar as possible, the terms and conditions should always be in a font size and spacing that facilitates easy reading.

The terms and conditions should disclose:

a. Details of the general charges;

b. The complaints procedure;

c. Information about any compensation scheme that the securities intermediary or CIU is a member of, and an outline of the action and remedies which the investor may take in the event of default by the securities intermediary or CIU;

d. The methods of computing interest rates paid or charged;

e. Any relevant non-interest charges or fees related to the product;

f. Any service charges;

g. Any restrictions on account transfers; and

h. The procedures for closing an account.
### Description

The following provisions in the Latvian laws provide for the obligations to make these disclosures:

- a. Article 127 (6)(4) of LFMI;
- b. Articles 127(13) and 126(1)(8) and (3) of LFMI;
- c. Article 9.2 of the Regulation regarding Distance Contracts for the Provision of Financial Services and Section 12(2) of the Investor Protection Law;
- d. Article 128(6)(4) of LFMI general obligation to disclose costs of services and Article 128(12) limits on fees that can be charged;
- e. Article 128(6)(4) of LFMI general obligation to disclose fees;
- f. Article 128(6)(4) of LFMI general obligation to disclose fees;
- g. There are no restrictions on transfers;
- h. Article 8 Regulation regarding Distance Contracts for the Provision of Financial Services.

There appears to be a disparity between the distance marketing rules and direct sales rules in that certain requirements for distance marketing disclosures are not in the requirements for direct sales.

### Recommendation

The marketing rules should be the same for all manner of sales activities to avoid any kind of regulatory arbitrage. The distance and direct marketing rules should be the same, except where unnecessary.

### Good Practice B.3

**Professional Competence**

Regulators should establish and administer minimum competency requirements for the sales staff of securities intermediaries and CIUs, and collaborate with industry associations where appropriate.

### Description

Under Article 128(4) of LFMI, the investment brokerage firm is responsible for selecting qualified people. However, there is no competency requirement or examination administered by the government or delegated to an association.

### Recommendation

A standard industry-wide examination for determining the competency of individual sales persons should be implemented by the FCMC or an industry association.

### Good Practice B.4

**Know Your Customer (KYC)**

Before providing a product or service to an investor, a securities intermediary or CIU should obtain, record and retain sufficient information to enable it to form a professional view of the investor’s background, financial condition, investment experience and attitude toward risk in order to enable it to provide a recommendation, product or service appropriate to that investor.

### Description

LFMI Article 126-2 provides for a "know your customer" rule that complies with MiFID.

### Recommendation

No recommendation.

### Good Practice B.5

**Suitability**

A securities intermediary or CIU should ensure that, taking into account the facts disclosed by the investor and other relevant facts about that investor of which it is aware, any recommendation, product or service offered to the investor is suitable to that investor.

### Description

LFMI Article 126-2 (10) provides for a suitability requirement that complies with MiFID. Article (12) states that it is not required in unsolicited trades for non-complex securities.

### Recommendation

No recommendation.

### Good Practice B.6

**Sales Practices**

Legislation and regulations should contain clear rules on improper sales practices in the solicitation, sale and purchase of securities. Thus, securities intermediaries, CIUs and their sales representatives should:
### Latvia

#### Securities Sector

**Good Practice B.7**

**Advertising and Sales Materials**

- All marketing and sales materials should be in plain language and understandable by the average investor.
- Securities intermediaries, CIUs and their sales representatives should ensure their advertising and sales materials and procedures do not mislead the customers.
- Securities intermediaries and CIUs should disclose in all advertising, including print, television and radio, the fact that they are regulated and by whom.

### Description

- Article 128(7) of LFMI requires that disclosures be made in a manner “so that customers or prospective customers can duly understand the essence of the offered investment service, ancillary (non-core) investment service and the particular type of the financial instrument and take appropriate decisions for making an investment.”
- LFMI Article 128(5) and Advertising Law Section 8(1) provide that misleading advertising is prohibited.
- Article 15.4 of the FCMC Regulations on information that, when providing investment services, should be given to customers regarding investment services, financial instruments, charges and performed transactions (available in Latvian) prescribes that when an investment firm gives information to a customer about itself and its investment services, the investment firm should disclose that it is licensed and by whom.

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**Latvia Securities Sector**

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<tbody>
<tr>
<td><strong>a.</strong></td>
<td>Not use high-pressure sales tactics;</td>
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<td><strong>b.</strong></td>
<td>Not engage in misrepresentations and half truths as to products being sold;</td>
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<tr>
<td><strong>c.</strong></td>
<td>Fully disclose the risks of investing in a financial product being sold;</td>
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<tr>
<td><strong>d.</strong></td>
<td>Not discount or disparage warnings or cautionary statements in written sales literature;</td>
</tr>
<tr>
<td><strong>e.</strong></td>
<td>Not exclude or restrict, or seek to exclude or restrict, any legal liability or duty of care to an investor, except where permitted by applicable legislation.</td>
</tr>
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</table>

Legislation and regulations should provide sanctions for improper sales practices.

### Description

- Section 4 of the Unfair Commercial Practices Prohibition Law prohibits aggressive tactics. Section 13 defines a number of extreme practices, including threats of violence. Section 13(3) includes delivery of “persistent and undesirable solicitations to the consumer, which have been expressed with the help of a telephone, fax, e-mail or other communication medium.”
- Section 9 of the Unfair Commercial Practices Prohibition Law prohibits misleading actions and Section 10 prohibits misleading omissions.
- Articles 128(6)(1)&(2) and (7) of LFMI require that investors be informed as to product services, risks and characteristics by an investment brokerage firm.
- There is no rule on disparagement.
- Section 5(4) of the Consumer Rights Protection Law prohibits any contract that attempts to limit a consumer’s legal rights as a violation of equality of rights.

The sanctions for improper sales practices are quite limited and include a warning and a fine of LVL 10,000 under Article 148 (5) and (8).

### Recommendation

The rule against disparagement is usually a fact question for a trial. Nonetheless it would be helpful if it were placed in the law as an element of investor protection. Even so, few, if any, jurisdictions have done this. The penalties for improper sales practices are weak and should be significantly strengthened.
<table>
<thead>
<tr>
<th>Recommendation</th>
<th>No recommendation.</th>
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**SECTION C  CUSTOMER ACCOUNT HANDLING AND MAINTENANCE**

**Good Practice C.1  Segregation of Funds**  
Funds of investors should be segregated from the funds of all other market participants.

**Description**  
LFMI Article 124(7) and (8) and Article 129 [in detail] and 129-1 all provide for the segregation of customer assets.

**Recommendation**  
No recommendation.

**Good Practice C.2  Contract Note**  
Investors should receive a detailed contract note from a securities intermediary or CIU confirming and containing the characteristics of each trade executed with them, or on their behalf. The contract note should disclose the commission received by the securities intermediary, CIU and their sales representatives.

**Description**  
LFMI Article 128(11) requires that a contract note (confirmation statement) be sent to a customer after a transaction and that FCMC regulations would define the content of the note. Article 31 of the FCMC Regulations on information that, when providing investment services, should be given to customers regarding investment services, financial instruments, charges and performed transactions (available in Latvian) prescribes the content of the confirmation statement..

**Recommendation**  
No recommendation.

**Good Practice C.3  Statements**  
An investor should receive periodic, streamlined statements for each account with a securities intermediary or CIU, providing the complete details of account activity in an easy-to-read format.

- a. Timely delivery of periodic securities and CIU statements pertaining to the accounts should be made.
- b. Investors should have a means to dispute the accuracy of the transactions recorded in the statement within a stipulated period.
- c. When an investor signs up for paperless statements, such statements should also be in an easy-to-read and readily understandable format.

**Description**  

a. LFMI Article 130-1 requires that a statement be sent to a client at least once a year - or more if agreed to with the client.

b. There is no specific procedure for disputing the accuracy of a transaction, although clients are allowed to complain through the complaint procedure.

c. There is no provision for this in Latvian law.

**Recommendation**  
The regulation should provide that those customers allowed to send in orders electronically should be allowed to receive their statements electronically in an easy-to-read and readily understandable format. Currently, investment firm and customer can agree to exchange information electronically (inter alia through electronic statements) in the agreement on investment services. The content of electronic statements should include the same information as paper statements.

**Good Practice C.4  Prompt Payment and Transfer of Funds**  
When an investor requests the payment of funds in his or her account, or the transfer of funds and assets to another intermediary or mutual fund, the payment or transfer should be made promptly.

**Description**  
According to the FCMC, orders should be promptly executed under LFMI Article 128(9). An order to transfer an account or receive funds would be covered by this provision. The FCMC was not aware of any problems in this area.
Recommendation | No recommendation.  

Good Practice C.5 | **Investor Records**  
A securities intermediary or CIU should maintain up-to-date investor records containing at least the following:  
a. A copy of all documents required for investor identification and profile;  
b. The investor’s contact details;  
c. All contract notices and periodic statements provided to the investor;  
d. Details of advice, products and services provided to the investor;  
e. Details of all information provided to the investor in relation to the advice, products and services provided to the investor;  
f. All correspondence with the investor;  
g. All documents or applications completed or signed by the investor;  
h. Copies of all original documents submitted by the investor in support of an application for the provision of advice, products or services;  
i. All other information concerning the investor which the securities intermediary or CIU is required to keep by law; and  
j. All other information which the securities intermediary or CIU obtains regarding the investor.  
Details of individual transactions should be retained for a reasonable number of years after the date of the transaction. All other records required under a. to j. above should be retained for a reasonable number of years from the date the relationship with the investor ends. Investor records should be complete and readily accessible.  

Description | LFMI Article 124 (9) and (10) requires that records be kept 10 years and that a records regulation will set out the details. The FCMC according to the Article 124 (1) 10 of LFMI has issued Regulations regarding the documents which an investment firm should store on compliance with the requirements of Chapter XII of LFMI (available in Latvian). According to the Article 124 (1) 10 the documents should be stored for 10 years. This regulation also covers items c, e, f and j.  
The Regulation for the Completion and Keeping of Source Documents associated with Financial Instrument Transactions covers this area for a, b, d, g, h, and i.  

Recommendation | No recommendation.  

SECTION D | PRIVACY AND DATA PROTECTION  

Good Practice D.1 | **Confidentiality and Security of Customers’ Information**  
Investors of a securities intermediary or CIU have a right to expect that their financial activities will have privacy from unwarranted private and governmental scrutiny. The law should require that securities intermediaries and CIUs take sufficient steps to protect the confidentiality and security of a customer’s information against any anticipated threats or hazards to the security or integrity of such information, and against unauthorized access to, or use of, customer information.  

Description | Article 124(6) of LFMI and Articles 131 and 132 of the Personal Data Protection Law require that customer information be kept confidential. Section 8 of the Personal Data Protection Law provides that this information should be provided to the customer at their request. Section 16 permits the investor to verify the accuracy of the information and supplement or correct it. If the data is out of date, incorrect or illegally obtained, the investor can demand that the data be destroyed.  

Recommendation | No recommendation.  

Good Practice D.2 | **Sharing Customer’s Information**  
Securities intermediaries and CIUs should:  
a. Inform an investor of third-party dealings in which they should share information regarding the investor’s account, such as legal enquiries by
### Latvia Securities Sector

| Description | a. Section 8 of Personal Data Protection Law provides that this information should be provided at the request of the subject.  

b. Section 8 of Personal Data Protection Law provides that this information should be provided at the request of the subject.  

c. Section 19 of the Personal Data Protection Law allows the investor to not give consent to sharing data for commercial purposes. It appears that it is common practice for customer agreements to allow the sharing of information within the different units of a financial conglomerate. |
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<tr>
<td><strong>Recommendation</strong></td>
<td>The Personal Data Protection Law should be amended to require the “data processor” to inform the investor how it uses and shares a customer's personal information.</td>
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</table>
| **Good Practice D.3** | **Permitted Disclosures**  
a. The law should state specific procedures and exceptions concerning the release of customer financial records to government authorities.  
b. The law should provide for penalties for breach of investor confidentiality. |
| **Description** | a. Articles 11 and 13 of the Personal Data Protection Law provides for the permitted disclosures for law enforcement, regulatory purposes, medical emergencies, legal proceedings and the like.  
b. The Personal Data Protection Law permits an aggrieved person to sue for any damages caused by the violation of the law by a data processor. The Data State Inspectorate can withdraw a data processing license and take unspecified administrative sanctions against a data processor for violations of the Law. |
| **Recommendation** | The sanctions need to be increased to provide a deterrent from violations of the Personal Data Protection Law. |

### SECTION E DISPUTE RESOLUTION MECHANISMS

| **Good Practice E.1** | **Internal Dispute Settlement**  
a. An internal avenue for claim and dispute resolution practices within a securities intermediary or CIU should be required by the securities supervisory agency.  
b. Securities intermediaries and CIUs should provide designated employees available to investors for inquiries and complaints.  
c. Securities intermediaries and CIUs should inform their investors of the internal procedures on dispute resolution.  
d. The securities supervisory agency should provide oversight on whether securities intermediaries and CIUs comply with their internal procedures on investor protection rules. |
|---|---|
| **Description** | a. Article 128 of LFMI requires that financial brokerage houses have an internal dispute resolution procedure.  
b. There is no legal requirement for a designated set of employees, although this appears to be common practice. The common practice at banks appears to be to have a general complaints procedure for all types of complaints and a specific unit within the bank designated to handle the complaints. |
### Good Practice E.2  
**Formal Claims Dispute Mechanisms**

There should be an independent dispute resolution system for resolving disputes that investors have with their securities intermediaries and CIUs.

- **a.** A system should be in place to allow investors to seek third-party recourse, such as an ombudsman or arbitration court, in the event the complaint with their securities intermediary or CIU is not resolved to their satisfaction in accordance with internal procedure, and it should be made known to the public.

- **b.** The independent dispute resolution system should be impartial and independent from the appointing authority and the industry.

- **c.** The enforcement mechanism of the decisions of the independent dispute resolution system and the binding nature of the decision on securities intermediaries and CIUs should be established and publicized rules.

### Description

- **a.** The Civil Procedure Law (Part D, Chapter 62, Section 490) allows for the creation of an Arbitration Court for a particular matter or for a standing court. The Association of Latvian Commercial Banks has a standing Court of Arbitration.

- **b.** However, the FCMC has instructed banks and investment brokerage firms not to put arbitration clauses in their contracts. The arbitration system has totally lost the trust of the Latvian public and is perceived as a biased decision-making mechanism. It is not considered to be an impartial and independent system. There is also an Ombudsman in the Association of Latvian Commercial Banks, but it only deals with complaints that relate to clearance, remittances or transactions involving electronic means of payment. As such, its jurisdiction is too limited to be an Ombudsman for the securities sector.

- **c.** The Civil Code provides for the enforcement mechanism of an arbitral award.

### Recommendation

There should be a system in place that allows an investor to seek affordable and efficient recourse to a third party in the event that the investor’s complaint is not resolved to the investor’s satisfaction under internal procedures of the securities intermediary or CIU. An alternative would be setting up a special division in the courts to handle financial disputes that would fast track small claims. This would create a cadre of judges experienced in these matters and would reduce costs for small claims while keeping standard procedures for large claims. Careful consideration should also be given to the establishment of a statutory independent ombudsman office for retail financial services, with a review of the costs and benefits of the scheme and a clear system established for the sustainable funding of such office.
<table>
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<tr>
<th>Description</th>
<th>financial instruments to investors by the insolvency trustee of a securities intermediary or CIU.</th>
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<tr>
<td>a.</td>
<td>The Law on the Financial and Capital Market Commission does not give the FCMC the authority to take corrective action directly regarding the insolvency of a financial brokerage firm. However, it can take action in regards to CIUs. It can change management companies or custodians to protect customer assets and, if that is not possible, it can order a liquidator for a CIU.</td>
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<tr>
<td>b.</td>
<td>The Investor Protection Law creates an investor guarantee fund that is administered by the FCMC. It is clear as to the instruments covered.</td>
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<tr>
<td>c.</td>
<td>The Investor Protection Law provides for a payout mechanism that is administered by the FCMC that appears to be effective, although it has not been used to the date of this diagnostic.</td>
</tr>
<tr>
<td>d.</td>
<td>There are no specific provisions for an investment brokerage firm in bankruptcy. On the other hand, there are specific provisions if a liquidator is needed for a CIU. Nonetheless, the investor guarantee fund will in theory provide the mechanism for prompt payment of investors with an investment brokerage firm and the investment fund segregation provisions should protect CIU investors. FCMC is confident that any payout required will be efficient and sufficient.</td>
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| Recommendation | No recommendation. |

**SECTION G**

**CONSUMER EMPOWERMENT**

**Good Practice G.1**

*Financial Education through the Media*

- a. Print and broadcast media should be encouraged to actively cover issues related to retail financial products.
- b. Regulators and/or industry association should provide sufficient information to the press and broadcast media to facilitate analysis of issues related to financial products and services.

<table>
<thead>
<tr>
<th>Description</th>
<th>a. There is an active local business media that follows developments in the stock market.</th>
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<td></td>
<td>b. The FCMC, CRPC and NASDAQ OMX Riga give interviews and information to the media on a regular basis.</td>
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</table>

| Recommendation | No recommendation. |

**Good Practice G.2**

*Information Resources for Investors*

- a. Financial regulators should devise, publish and distribute information resources for investors that seek to improve awareness, providing independent information on the costs, risks and benefits of financial products and services.
- b. Non-governmental organizations should be encouraged to provide investor awareness programs to the public regarding financial products and services.

<table>
<thead>
<tr>
<th>Description</th>
<th>a. The FCMC does not engage in distribution of information resources for investors other than a general web page. The NASDAQ-OMX Riga has an investor awareness website that is more extensive.</th>
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<tr>
<td></td>
<td>b. There is no NGO or professional association that is currently active in the securities sector in the area of investor awareness and education.</td>
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| Recommendation | More investor education should be encouraged by the regulatory authorities, but due to the small size of the market this effort will probably be limited. |
Latvia: Consumer Protection in the Credit Reporting System

Overview

The coverage and depth of information of the credit reporting system in Latvia lags behind the most advanced EU New Member States (NMS). The overall coverage of adult population reached 3.7 percent or about 875,000 persons as of March 31, 2009¹ and was significantly below the average of other European countries, including Estonia and Lithuania. Also, based on the most recent Doing Business statistics (2009), Latvia’s credit reporting system scored 4 out of 7 in terms of depth of credit information, lagging behind most of the NMS. The statistics on coverage and depth are based on the information of the Credit Register operated by the Bank of Latvia. The Credit Register collects both positive and negative credit information from banks and their subsidiaries that provide credit, insurance companies and credit unions, as well as the Motor Insurers’ Bureau of Latvia. Although about four debt collection companies and several non-bank credit institutions that operate in Latvia store data about their clients’ credit history—acting as de facto private credit bureaus—the information held is not accounted in any official statistics.

The low performance in terms of coverage and depth is explained by the recent establishment of the Credit Register, fully operational since July 2008. The borrowers’ credit data previously registered in the Bank of Latvia’s Register of Debtors, which only contained negative information, was automatically transferred to the Credit Register developed in the Payment Systems Department of the Bank of Latvia. Since July 2008 when all Credit Register’s participants submitted complete data on credit portfolio, the Register receives negative and positive credit information on borrowers and their guarantors for every new loan or amendments to loans extended by the Register’s participants. The information covers data on obligations, data on the outstanding obligations at the end of the calendar quarter, debtor information, information on the modified and cancelled data as well as information on data requests.

¹ Data released by the Credit Register of the Bank of Latvia.
Given the recent establishment of the Credit Register, coupled with the overall decrease of new loans, no trend in usage could be establish at this stage to suggest the increased importance of credit records in managing lending portfolios. To date the Credit Register comprises data about 875,000 credit beneficiaries, of which about 827,000 are natural persons. The data is collected from 111 participant institutions (27 banks, 25 companies having close links with banks, 24 insurance companies and 35 credit unions). By January 2009, the outstanding balance of loans reported to the Register totaled LVL 17.7 billion. During the first quarter of 2009 banks conducted 833,000 inquiries in the Register and about 750 persons requested information regarding their own records.

**Legal Framework and Institutional Arrangements**

The list of principal laws and regulations concerning credit reporting systems activities include:

- Personal Data Protection Law (effective 6 April 2000, amended in 2002 and 2006);
- Obligatory Technical and Organizational Requirements for Protection of Personal Data Processing System, Cabinet Regulation No. 40/2001;
- Credit Institutions Law (effective 1 January 2007, as last amended in February 2007);
- Credit Union Law (effective January 1 2002, amended 20 Nov, 2003);
- Law on Insurance Companies and Supervision Thereof;
- Law on Civil Liability Insurance for Land Vehicle Owners;
- Regulation for the Credit Register, Bank of Latvia Regulation No. 32/2009;
- Technical Regulation for the Credit Register, Bank of Latvia Regulation No. 33/2009;
- The Amount of and the Payment Procedure for the Fees to Be Paid for the Use of the Credit Register by Its Participants, Bank of Latvia Regulation No. 34/2009 ;
- Consumer Rights Protection Law (March 1999, as last amended in June 2009)

The Credit Register is a public register established in January 2008 that enables participant institutions (banks and their subsidiaries providing financial services associated with credit risks, credit unions, insurance companies as well as the Motor Insurers’ Bureau of Latvia) to asses borrowers’ credit worthiness more accurately and manage credit risks more efficiently. The Credit Register is maintained by the Payment Systems Department of the Bank of Latvia and provides information to the Financial and Capital Market Commission (FCMC) and the Bank of Latvia for performing supervisory and analytical functions. Consumers can receive, free of charge, data pertaining to their own credit history. The Credit Register collects, accumulates and stores data on the borrowers and borrower guarantors, their liabilities and performance thereof, including the data on any new loan granted, on settlement of liabilities, delayed payments and violations of the contractual terms..

The Data State Inspectorate (DSI) was established by the Personal Data Protection Law to ensure the protection of individuals in the processing and access of their personal data, and to monitor the observance of the Law. The DSI is supervised by the Ministry of Justice and is organized as a state administration institution whose management is appointed and released from function by the Cabinet, at the proposal of the Minister of Justice. The law provides that DSI operates independently, takes decisions and issues administrative acts; however the legal status of DSI creates concerns regarding its de facto independence and effectiveness. Independence is one of the main requirements by the EU Data Protection Directive and international standards. This concern was partially addressed by the concept of the “Status of Independent Institution” adopted by the Cabinet of Ministers, which includes the DSI as one of the institutions whose effective functioning can be seriously undermined if working within the institutional structure of subordination and therefore political power. The last necessary step will be amendments in the Constitution (Art. 58 of Satversme).
DSI is charged with making decisions and reviewing complaints, making formal recommendations, issuing permission for the transfer of information abroad, and maintaining and inspecting the national register of data processing systems. DSI is also authorized to impose administrative penalties for violations of personal data processing rules and to bring to Court violations of the Personal Data Protection Law. DSI registers all natural or legal persons that process personal data and establish systems for personal data processing. DSI prepares annual reports of activity that are submitted to the Cabinet and are published in the Official Gazette.

**Key Recommendations**

The main recommendations for improving consumer protection and financial capability in the area of credit reporting systems are:

- When a consumer is asked to consent to sharing his or her personal data with a credit bureau, the consumer should receive a brochure, supplied by the bureau, explaining its data handling and sharing procedures in a simple way (diagram).
- The pricing of the loan including the credit risk premium that the consumer is charged and its calculation should be clearly communicated to the consumer. This should include reference to any information (credit history factors) obtained from the credit reporting system.
- The Credit Register should red flag credit information under dispute. The reporting institutions should be required to flag or temporarily withdraw any disputed information, and be obliged to resolve the disputed information within a certain period or initiate an out-of-court settlement process.
- To avoid a potential negative evaluation by creditors, private credit bureaus should not include in their reports information on the number of inquiries made by an individual for credit, but only the number of rejected loan applications if desired. Consumers should also be able to obtain individual loan pricing without submitting formal application for a loan.
- The credit scoring system (methodology) of the companies that act as de facto private credit bureaus should be reviewed by the Bank of Latvia and CRPC, and its main features communicated to the public so that consumers are encouraged to engage in active credit history management.
- Client history should be enhanced by allowing the participation of NBCIs to the Credit Register. This is also important for current participants to the Credit Register because the Credit Register is expected not to provide a credit scoring of consumers in the future. Credit scoring provided by some of the NBCIs that act as de facto private credit bureaus could have a positive effect on the availability and cost of credit for consumers.
- The Credit Register should further collect reports on consumers’ payment discipline from utility companies and telephone operators and cable TV providers.
- The Data State Inspectorate should publish, in a consolidated manner, information on complaints concerning violation of personal data protection in financial services to inform and educate the public in the area of financial services. It should also resume the publication of the Annual Report on the website, practice interrupted in 2006.
- The Credit Register should have clearly defined responsibilities and resources for raising public awareness about the importance of maintaining a good credit history and its impact on the borrowing cost and access to finance. Also, the Credit Register and de facto credit bureaus should, in cooperation with the Data State Inspectorate, inform and educate the public about key issues on personal data protection in financial services. The websites of the Credit Register and credit bureaus should include information on consumers’ rights, as well as procedures to obtain a copy of the information that the Credit Register or bureau maintains on them.
## Good Practices: Credit Reporting System

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<th>SECTION A</th>
<th>PRIVACY AND DATA PROTECTION</th>
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<td>Good Practice A.1</td>
<td><strong>Consumer Rights in Credit Reporting</strong></td>
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Laws and regulations should require basic consumer rights. These rights may include:

- a. The right of the consumer to consent to information-sharing based upon the knowledge of the institution’s information-sharing practices.
- b. The right to access the credit report of the individual, subject to proper identification of that individual and free of charge (at least once a year).
- c. The right to know about adverse action in credit decisions or less-than-optimal conditions/prices due to credit report information. In this process, consumers should be provided with the name and address of credit bureau.
- d. The right to be informed about all inquiries within a period, such as six months.
- e. The right to correct factually incorrect information or to have it deleted.
- f. The right to mark (flag) information that is in dispute.
- g. The right to decide if the consumer’s credit information (for purposes not related to the granting of credit) can be shared with third parties.
- h. The right to have sensitive information especially protected (not included in the credit report), such as race, political and philosophical views, religion, medical information, sexual orientation or trade union membership.
- i. The right to reasonable retention periods such as those for positive information (for example, at least two years) and negative information (for example, 5-7 years.)
- j. The right to have information kept confidential and with sufficient security measures in place to prevent unauthorized access, misuse of data, or loss or destruction of data.
- k. Credit registers should refrain from negatively taking into account any of the consumer rights granted in calculating credit scores or for otherwise inferring creditworthiness.
- l. The number of inquiries by an individual on credit pricing should be evaluated in a way that allows for comparison shopping without negatively impacting on the credit score.

### Description

There is a clear legal framework with respect to consumer rights in credit reporting. Thus, the operation of the public credit register (the Credit Register maintained by the Bank of Latvia) is regulated by the Credit Institutions Law, the Regulations of the Bank of Latvia no. 32/2009, no. 33/2009, and no. 34/2009 and the Personal Data Protection Law. The legal framework for establishment and operations of private credit bureaus is less specific. Their establishment is governed by the Commercial Law, and their operations are subject to registration by the Data State Inspectorate (DSI) and governed by the Personal Data Protection Law. The key provisions regarding consumer protection in laws and regulations applicable to credit reporting are listed below.

**Personal Data Protection Law (effective 1 January 2002 and amended on 24 October 2002 and 19 December 2006):** The objective of the Law is to protect the fundamental human rights and freedoms of natural persons, in particular the inviolability of private life, with respect to the processing of personal data. The Law applies, inter alia, to processing of personal data that are designed to become part of a credit register. The controller needs to ensure that the following are complied with: (i) the personal data processing takes place with integrity and lawfully; (ii) the personal data is processed only in conformity with the intended purpose and to the extent required therefore; (iii) the personal data is stored so that the data subject is identifiable during a relevant period of time, which does not exceed the time period prescribed for the intended purpose of the
data processing; and (iv) the personal data are accurate and they are updated, rectified or erased in a timely manner if such personal data are incomplete or inaccurate in accordance with the purpose of the personal data processing.

Cabinet of Ministers Regulation No. 40/2001 on the Obligatory technical and organizational requirements for protection of personal data processing systems:
This regulation defines obligatory technical and organizational requirements for protection of personal data processing systems. Inter alia, the personal data processing system administrators need to ensure that: (i) processing personal data as collection, storage, modification, correction, deleting, elimination, archiving, reserve copying, blocking, needs to be done exclusively by authorized persons; (ii) processing systems should also have the capability to track down unauthorized data processing, including the processing time and the person which processed personal data.

Credit Institutions Law (effective 1 January 2007, most recently amended 22 February 2007): Article 106 (paragraphs 4, 5, 6) defines the credit institutions that are participants to the Credit Register.

Regulations of the Bank of Latvia No, 32/2009, 33/2009 and 34/2009 define the operational regulations for the Credit Register and its participants.

a. The right of the consumer to consent to information-sharing based upon the knowledge of the institution's information-sharing practices. The Credit Institutions Law (Article 106) provides that all banks, as well as their subsidiaries are required to submit information to the Bank of Latvia regarding the debtors and the course of fulfillment of their commitments. The Law also indicates in Article 62 that information regarding a customer, his or her accounts and transactions, shall be provided to third parties only if the customer has unequivocally consented to provide such information with an agreement entered into with the credit institution. The Personal Data Protection Law (Section 7, Articles 1 and 2 and Section 8) states that personal data processing is permitted only if, among other conditions, at least one of the following is met: (i) consumers give his or her consent for personal data processing; (ii) such personal data processing results from contractual obligations or, taking into account a request from the data subject, the processing of data is necessary in order to enter into the relevant contract. The consent should be a freely, unmistakably expressed affirmation of the wishes of a data subject, by which the data subject allows his or her personal data to be processed. Thus, when collecting personal data from a data subject, a system administrator has a duty to provide a data subject with the following information unless it is already available to the data subject: (i) the designation, or given name and surname, as well as address of the system administrator and the personal data operator; and (ii) the intended purpose and basis for the personal data processing. The Law (Section 8) also provides that only based on a specific written request the consumer has the right to be informed about the possible recipients of the personal data. Private credit bureaus are not covered by special law or regulations, but they must follow the provisions of the Personal Data Protection Law and obtain the customer’s consent as described above.

b. The right to access the credit report of the individual, subject to proper identification of that individual and free of charge (at least once a year). The Bank of Latvia Regulation No. 32 (Article 14) provides that credit institutions participant to the Credit Register need to inform the customer and its guarantor about the credit information that would be stored in the Credit Register. Also, according to Article 36 any person is entitled to receive directly from the Credit Register, free of charge, all information stored regarding their credit history. The information is issued within five working days from the submission of a written request and is handed personally in hard copy, subject to proper identification based on the person’s valid identity document. Non-bank institutions that operate as private credit registers are subject to the Personal Data Protection Law, which states that customers have the right to gain access to his or her personal data;

c. The right to know about adverse action in credit decisions or less-than-
optimal conditions/prices due to credit report information. In this process, consumers should be provided with the name and address of credit bureau. The Credit Institutions Law is silent on the right to know about adverse action in credit decisions or less-than-optimal conditions/prices due to credit report information. However, in practice, banks inform the customer if he is denied credit (though this information will not necessarily state that the credit report was the deciding factor). While banks will price a loan according to information in the credit report, they need not inform the consumer that the price depends on the credit report information. The law is silent on the need to provide the consumer with the name and address of the Credit Register or private credit bureau whose information was used in the credit decision.

d. The right to be informed about all inquiries within a period, such as six months. Regulation 32 of the Bank of Latvia gives the right to the consumer to be informed about all inquiries made on him or her. The credit institutions participant to the Credit Register do not receive information on inquiries made by other credit institutions.

e. The right to correct factually incorrect information or to have it deleted. The Personal Data Protection Law (Section 16) provides that customers have the right to request that his or her personal data be supplemented or rectified by the system administrators (e.g. financial institutions), as well as that their processing be suspended or that the data be destroyed if the personal data are incomplete, outdated, false, unlawfully obtained or are no longer necessary for the purposes for which they were collected. If the data subject is able to substantiate that the personal data included in the personal data processing system are incomplete, outdated, false, unlawfully obtained or no longer necessary for the purposes for which they were collected, the system administrator has an obligation to rectify this inaccuracy or violation without delay and notify third parties (e.g. credit registers) who have previously received the processed data of such. If information has been retracted, the system administrator shall ensure the accessibility of both the new and the retracted information, and that the information referred to is received simultaneously by recipients thereof. According to Regulation 32, any person has the right to verify the information relating to him in the Register, including the names of the banks and their subsidiary financial institutions which have submitted the information to the Credit Register. Upon a legitimate request from a customer, the Bank of Latvia provides the requested information within five working days. If a person considers that the information in the Register is incorrect, he or she may request that the information be adjusted or updated by the credit institution which has submitted it to the Register. No longer than one working day (Article 21) from receipt of the request, the institution in question must send an instruction to the Credit Register to make the necessary adjustments.

f. The right to mark (flag) information that is in dispute. Regulation 32 is silent on the right to mark (flag) information that is in dispute, and this is not done in practice by the Credit Register.

g. The right to decide if the consumer’s credit information (for purposes not related to the granting of credit) can be shared with third parties. In accordance with Regulations 32 and 34, the Credit Register shall provide participant credit institutions with information on the credit history of particular customers against the payment of a fee. Articles 38-40 of Regulation 32 provide that Credit Register participants are entitled to receive the information collected on the Credit Register’s database, in a manner which does not directly or indirectly identify a borrower or borrower’s guarantor and the participants that submitted information in the Register. The FCMC has also the right to receive aggregated information of the Credit Register in a manner which does not directly or indirectly identify a borrower or borrower’s guarantor. The Credit Register can provide information only to the participant credit institutions. Private credit bureaus may release data to other credit institutions only based on a prior consent from the customer as per the Personal Data Protection Law.
h. The right to have sensitive information especially protected (not included in the credit report), such as race, political and philosophical views, religion, medical information, sexual orientation or trade union membership. The Personal Data Protection Law (Section 11) forbids processing sensitive personal data which indicate race, ethnic origin, religious, philosophical or political convictions, or trade union membership of a person, or provide information as to the health or sexual life of a person unless the data subject has given his or her written consent for the processing of his or her sensitive personal data. The circumstances provided in the Law as exceptions would not apply to a credit registry or credit bureau.

i. The right to reasonable retention periods such as those for positive information (for example, at least two years) and negative information (for example, 5-7 years). Regulation 32 (Article 12) requires that information in the Credit Register be stored permanently, with no distinction between retention periods of positive and negative information. The private credit bureaus retain only negative information and for a period reported of at least 10 years (period in which cases could be disputed in courts).

j. The right to have information kept confidential and with sufficient security measures in place to prevent unauthorized access, misuse of data, or loss or destruction of data. Regulation No. 40 defines obligatory technical and organizational requirements for protection of personal data processing systems, which apply to inter alia credit institutions, non-bank credit institutions, the Credit Register, as system administrators at the DSI. General provisions for protecting personal data processing systems are covered by the Regulation No. 106 of Cabinet of Ministers on Security Regulations for Information Systems. The Credit Institutions Law states that credit institutions have the duty to guarantee the confidentiality of the identity, accounts, deposits and transactions of their customers (Article 61). Such information can only be disclosed under specific circumstances (enumerated in Article 63) to state institutions, state officials or other institutions and officials. Intentional or non-intentional disclosure of such information falls under criminal procedure and applies equally to current and former employees of the credit institution, FCMC, Bank of Latvia or any other state institution or official that had access to such information.

k. Credit registers should refrain from negatively taking into account any of the consumer rights granted in calculating credit scores or for otherwise inferring creditworthiness. The law is silent on this subject matter. However, the Credit Register does not currently calculate credit scores and is not planning to do so in the future either. However, some of the NBCIs that act as de facto private credit bureaus do provide credit scoring.

l. The number of inquiries by an individual on credit pricing should be evaluated in a way that allows for comparison shopping without negatively impacting on the credit score. The law is silent on this subject matter. However, the current contents of the Credit Register’s reports do not include any information on the number of customer inquiries. Hence, no effect from comparison shopping would be included.

Recommendation

When a consumer is asked to consent to sharing his or her personal data with a credit bureau, the consumer should be provided with a brochure explaining the bureau’s data handling and sharing procedures in a simple way (diagram).

The consumer should receive clear information on the pricing of a loan, including the credit risk premium that the consumer is charged and references to any information (credit history factors) obtained from the Credit Register or a private credit bureau. Disclosure of such information is important for educating consumers about the relationship between credit history and borrowing costs, and helping uncover errors in credit reports that did not result in rejected applications but higher borrowing costs.

The Credit Register should red flag credit information under dispute. The reporting
Institutions should be required to flag or temporarily withdraw any disputed information. They should also be obliged to resolve the disputed information within a certain period (e.g., seven days) or initiate an out-of-court settlement process.

The credit scoring system (methodology) of the NBCIs that act as *de facto* private credit bureaus should be reviewed/approved by the Bank of Latvia and CRPC and its main features communicated to the public so that consumers are encouraged to engage in active credit history management.

Client history should be enhanced by allowing the participation of NBCIs to the Credit Register. This is important for current participants to the Credit Register because even if the Credit Register records both positive and negative information and further expands the information of consumers’ credit history, it is expected not to provide a credit scoring of consumers in the future. Credit scoring provided by some of the NBCIs that act as *de facto* private credit bureaus could have a positive effect on the availability and cost of credit for consumers. The Bank of Latvia should develop and communicate a long-term strategy for the Credit Register and its targeted ultimate information content/structure. The Credit Register should further collect reports on consumers’ payment discipline from utility companies and telephone operators and cable TV providers.

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<thead>
<tr>
<th>Good Practice A.2</th>
<th>Preservation of Rights</th>
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<td>Participants of the credit reporting system (credit registers, reporting institutions and others) should not, in any communication or agreement with a consumer (except where permitted by applicable legislation), exclude or restrict, or seek to exclude or restrict:</td>
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<tr>
<td>a. Any legal liability or duty of care to a consumer provided under the applicable law or regulations;</td>
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<tr>
<td>b. Any duty to act with skill, care and diligence owed to a consumer in connection with the provision of the financial services or products; or</td>
<td></td>
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<tr>
<td>c. Any liability arising from the failure to exercise the degree of skill, care and diligence that may reasonably be expected of the participants in the provision of financial services.</td>
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| Description | As described in the Banking Section, the Civil Code establishes some provisions regarding professional duty, but there is no explicit provision in Latvian law regarding preservation of duty of care for participants of the credit reporting system. |

| Recommendation | The provisions of this good practice should be incorporated into Latvian legislation. |

<table>
<thead>
<tr>
<th>Good Practice A.3</th>
<th>Institutional Framework</th>
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<tr>
<td>a. There should be a general consumer agency or specialized agency responsible for implementing, overseeing and enforcing the protection of personal data.</td>
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<td>b. The authority should monitor complaints, disputes and inquiries and have a register which lists the names of credit registers.</td>
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<tr>
<td>c. The authority should be able to conduct audits in credit registers, including regular reviews of data quality and completeness in credit registers.</td>
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<tr>
<td>d. The legal system should provide for a role for the private sector, including voluntary consumer protection organizations and self-regulatory organizations.</td>
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<tr>
<td>e. Where oversight and enforcement of credit register laws are the responsibility of several authorities, there should be clear rules for interagency consultation and cooperation. There should be regular meetings between experts in charge, located at different agencies.</td>
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<tr>
<td>f. Credit registers should have the duty to register or obtain a license from the regulator.</td>
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| Description | a. There should be a general consumer agency or specialized agency responsible for implementing, overseeing and enforcing the protection of personal data. The Data State Inspectorate (DSI) is a specialized agency in Latvia empowered by the Personal |
Data Protection Law to ensure the protection of individuals in the processing and access of their personal data, and to monitor the observance of the Law. In accordance with Section 29 (1), DSI operates independently, takes decisions and issues administrative acts.

b. The authority should monitor complaints, disputes and inquiries and have a register which lists the names of credit registers. DSI is charged with making decisions and reviewing complaints, making formal recommendations, issuing permission for the transfer of information abroad, and maintaining and inspecting the personal data processing systems. DSI is also authorized to impose administrative penalties for violations of personal data processing, to cancel personal data registration certificate of processing systems and to bring to Court violations of the Personal Data Protection Law. DSI registers all natural or legal persons that establish systems for personal data processing. The register for personal data processing systems is a component of the State information system.

Section 29(3) of the Personal Data Protection Law outlines the duties of the DSI: (i) to ensure compliance with this Law; (ii) to take decisions and review complaints regarding the protection of personal data; (iii) to register personal data processing systems; (iv) to propose and carry out activities aimed at raising the efficiency of personal data protection and submit reports on compliance of personal data processing systems created by national and local government institutions; (v) together with the Office of the Director General of the State Archives of Latvia, to decide on the transfer of personal data processing systems to the State archives for preservation thereof; (vi) to accredit persons wishing to perform system auditing of personal data processing systems of national and local government institutions in accordance with procedure established by the Cabinet of Ministers. The obligations of the DSI to examine complaints and adopt decisions in relation to personal data protection has been the most significant function of DSI, which in most cases has been based on complaints from individuals on possible infringement of privacy. To examine submissions or complaints the DSI carries out controls and, if violations of the Law are detected, it adopts decisions and/or applies administrative sanctions if necessary. The procedure for handling complaints is set forth in the Administrative Procedure Law, unless a different procedure is stipulated by special legislations.

c. The authority should be able to conduct audits in credit registers, including regular reviews of data quality and completeness in credit registers. DSI is empowered to (i) freely enter any non-residential premises where personal data processing systems are located, and in the presence of a representative of the system administrator carry out necessary inspections or other measures in order to determine the compliance of the personal data processing procedure with law; (ii) to require written or verbal explanations from any natural or legal person involved in personal data processing; (iii) to require that documents are presented and other information is provided which relate to the personal data processing system being inspected; (iv) to require inspection of a personal data processing system, or of any facility or information carrier of such, and to determine that an expert examination be conducted regarding questions subject to investigation; (v) to request assistance of officials of law enforcement institutions or other specialists, if required, in order to ensure performance of its duties; (vi) to prepare and submit materials to law enforcement institutions in order for offenders to be held liable, if required; and (vi) to draw up a statement regarding administrative violations in personal data. The annual reports of the DSI include cases of violation of the Personal Data Protection Law and relevant statements of the DSI. The practice of publishing annual reports and statements of DSI was discontinued since 2006.

d. The legal system should provide for a role for the private sector, including voluntary consumer protection organizations and self-regulatory organizations. The Consumer Rights Protection Law provides consumer associations with a clear role in consumer rights protection. Consumer associations have the right to: (i) participate, together with supervisory and control institutions for consumer rights, in inspections of quality compliance to providers of goods and services; (ii) examine complaints and proposals from consumers and provide assistance when consumer rights have been violated; and (iii) submit statements of claim to courts related to protection of consumer rights and represent the consumer's interest in court. The Personal Data Protection Law does not provide any specific role to consumer associations.
e. Where oversight and enforcement of credit register laws are the responsibility of several authorities, there should be clear rules for interagency consultation and cooperation. There should be regular meetings between experts in charge, located at different agencies. There is no specific legal framework for private credit bureaus. However, the Personal Data Protection Law provides the DSI with the authority to request assistance of officials of law enforcement institutions or other specialists, if required, in order to ensure performance of its duties.

f. Credit registers should have the duty to register or obtain a license from the regulator. The Personal Data Protection Law requires all personal data system administrators to be registered by DSI. Chapter IV, Registration and Protection of a Personal Data Processing System, states that institutions, inter-alia, credit institutions, credit register and companies that have systems to process personal data that may also include credit records, need to register at DSI by observing the following procedures:

- **Application**: The application for registration includes: (i) the designation (name and surname), registration code, address and telephone number of the institution or person (system administrator); (ii) the name, surname, personal identity number, address and telephone number of a person authorised by the system administrator; (iii) the legal basis for the operation of the personal data processing system; (iv) the type of personal data to be included in the system, the purposes for which it is intended and the amount of personal data to be processed; (v) the categories of data subjects; (vi) the categories of recipients of personal data; (vii) the intended method of personal data processing; (viii) the planned method of obtaining personal data and a mechanism for the control of their quality; (ix) other data processing systems, which will be connected with the system to be registered; (x) the type of personal data that connected systems will be able to obtain from the system to be registered, and the type of data that the system to be registered will be able to obtain from connected systems; (xi) the method for transferring data from the system to be registered to another system; (xii) the identification codes of natural persons as will be used by the system to be registered; (xiii) the method for exchanging information with the data subject; (xiv) the procedures whereby a personal data subject is entitled to obtain information concerning himself or herself; (xv) the procedures for supplementing and updating personal data; (xvi) technical and organisational measures ensuring the protection of personal data; and (xvii) the type of personal data that will be transferred to other states.

- **Evaluation**: DSI evaluates and determines the personal data processing systems in which a prior checking must be performed.

- **Certification**: DSI issues a certificate of registration of the personal data processing system to a system administrator or to a person authorised by him or her.

- **Registration of changes**: Prior to changes being made in a personal data processing system, such changes need to be registered in the DSI. The following types of changes need to be recorded: (i) the system administrator or the personal data processor; (ii) the location of the personal data processing system; (iii) the types of personal data or the purpose of the personal data processing; (iv) the holder of the information resources or technical resources, as well as the responsible person for the security of the information system; (v) the data processing systems with which the relevant system is associated; (vi) the type of personal data processing; and (vii) the type of personal data processing, which is transferred to other states.

The DSI does not organize the register of data processing systems in a manner that allows the identification of the companies that act as private credit registers.

**Recommendation**

The annual reports of the companies that act as *de facto* private credit bureaus should be reviewed by the DSI and the Bank of Latvia on a no objection basis. The annual reports of each credit bureau should be published on the bureau's website and disseminated via
financial institutions branches as part of a program on raising awareness and educating financial consumers about the credit bureaus' activities and performance.

The DSI needs to continue the practice stopped in 2006 of publishing, in a consolidated manner, information on the complaints concerning violation of personal data protection in financial services, in order to inform and educate the public in the area of financial services.

**SECTION B**

**CONSUMER EMPOWERMENT**

**Good Practice B.1**  
*Information Resources for Consumers*

Financial regulators should devise, publish and distribute information resources for consumers that seek to improve their knowledge of actively managing the credit report.

**Description**

The Credit Register is not actively involved in this subject matter. The website of the Bank of Latvia contains information on the regulations governing the functioning of the Credit Register. However, there is no window with information for consumers on their rights, or procedures to obtain a copy of the information that the Credit Register maintains on them. Nor is such information distributed through participating institutions.

**Recommendation**

The Credit Register, as a public institution, should have a clearly defined budget for raising public awareness about the importance of good credit history and its impact on the borrowing cost and access to finance. Also, the Credit Register and companies that act as *de facto* credit bureaus should, in cooperation with the Data State Inspectorate, inform and educate the public about possible threats regarding misuse of personal data in financial services and how to improve own personal data security in regards to personal finance. The websites of the Credit Register and credit bureaus should include information for consumers on their rights, as well as the procedures to obtain a copy of the information that the Credit Register or bureau maintains on them.

Similarly the Data State Inspectorate should include on its website a list of the private credit registers and inform the customers on the data processed by them.

**Good Practice B.2**  
*Awareness of Credit Reporting*

In order to ensure that financial consumer protection and educational initiatives are appropriate, it is necessary to measure financial capability with large-scale surveys that are repeated periodically. These surveys should include questions on credit reporting and scoring.

**Description**

Please see Banking Section, Good Practice G.5.

**Recommendation**

Please see Banking Section, Good Practice G.5.
Latvia: Consumer Protection in the Insurance Sector

Overview

The Latvian insurance market has experienced a strong growth in recent years, except in 2008 when it became affected by the financial crisis. However, both life and non-life insurance markets remain small in relative terms, with the non-life segment being the smallest in Europe. Globally, the Latvian insurance market’s size ranked 80th in 2006, between Jordan and Sri Lanka. Total premium income of the Latvian insurance market in 2008 was about LVL 350 million compared with less than LVL 130 million in 2003, a growth of over 160 percent. The exceptional growth was recorded in the life insurance segment, due to the lower initial penetration and increasing income levels in the years preceding 2008, with a greater number of middle-class households purchasing life insurance products as savings instruments. In 2008 the overall sector continued to grow although a drop of about 8 percent was registered in the life insurance segment. Further decline is expected due to lower income and saving levels. It is reasonable to expect lower rates in the non-life insurance segment as well given deteriorating business activity and substantial drops in car loans and mortgages. The average annual growth rate of the insurance sector from 2003 to 2008 was 23 percent, with the life insurance segment growing at about 40 percent on average.

Figure 13: Latvian Insurance Market Growth (2004-2008)

Total assets of the insurance market have also increased in recent years, reaching almost LVL 400 million or USD 0.8 billion at end-2008. Total assets of the insurance industry have grown by 155 percent since 2004. Assets continued to grow in 2008, with an annual growth rate of around 20 percent in both life and non-life segments.

Total assets of the insurance market have also increased in recent years, reaching almost LVL 400 million or USD 0.8 billion at end-2008. Total assets of the insurance industry have grown by 155 percent since 2004. Assets continued to grow in 2008, with an annual growth rate of around 20 percent in both life and non-life segments.

Despite the industry’s growth in recent years, the development of Latvia’s insurance market lags behind other EU New Member States (NMS). Latvia remains behind other NMS both in terms of insurance penetration and density (premiums per capita). Insurance penetration has remained at about 2 percent of GDP between 2003 and 2008. This level is lower than the NMS average of 3.2 percent and the EU-15 average of 9.9 percent. With an insurance density of USD 300 in 2008, Latvia lags behind most of the NMS and EU-15 countries. The average insurance density of the EU-15 for 2008 was USD 3,960.
The insurance market in Latvia is dominated by the non-life segment. Non-life premium volumes grew by an average of 22 percent annually over 2003-2008. In 2008 the non-life insurance market grew by about 13 percent relative to 2007, a slowdown from its 2007 annual growth rate of 50 percent. By the end of 2008 the non-life gross written premiums amounted to LVL 300 million. The non-life insurance business has grown along with the overall economy over time. The recent growth of the non-life segment resulted from purchases of new vehicles (financed by borrowing) as well as increases in rates for compulsory motor third party liability (MTPL), where results had been very poor in previous years because of low rates and frequent claims. Another reason of growth is the expansion of the domestic mortgage and car leasing sectors. However, there has been a slight deterioration of premium income in property and land vehicle insurance products, which may continue throughout 2009 due to the deterioration of household incomes and the decrease in loans to households and private sector.

Figure 17: Structure of Non-Life Insurance Premium Income by Product
(in percentage, December 2008)

Source: FCMC

The dominant product of the non-life insurance segment is auto insurance. In 2008 premium income for auto insurance products accounted for 59 percent of total non-life insurance products; 33 percent for land vehicles and 26 percent for MTPL. MTLP increased its participation in the non-life segment from a share of 22 percent in 2007. The second largest line of business in the non-life segment is property insurance, which accounted for 15 percent of non-life premiums in 2008, followed by health insurance (13 percent).

The non life insurance market has remained highly concentrated over time. There has been little change in market concentration over the last five years. The market share of the top five insurers increased from 72 percent in 2003 to 75 percent in 2007. Major players in the market include BTA (Baltijas Transporta Apdrosinasana until 2004), Balta, Gjensidige Baltic (Parekss Apdrosinasanas Kompanija until 2007), Balva and If Latvia. Some insurers have a strategic investment from European insurance companies (Codan from Denmark, Ergo from Germany, Gjensidige from Norway) while some have institutional investors as major shareholders (BTA). One company (Baltikums) is bank-owned.

Early market expansion was based on privatization, organic growth and foreign investments. Only after 2006 acquisition and merger activities started playing a larger role with Norwegian insurer Gjensidige buying Parekss insurance company and Nordens acquiring Balva in 2007. In the same year Swedish insurer LF announced the establishment of a new branch in Latvia operating under the name Nordicia184.

### Table 9: Non-Life Insurance Market Concentration

<table>
<thead>
<tr>
<th></th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
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<tbody>
<tr>
<td>Top five companies</td>
<td>72</td>
<td>73</td>
<td>72</td>
<td>75</td>
<td>75</td>
</tr>
<tr>
<td>Top ten companies</td>
<td>98</td>
<td>98</td>
<td>99</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: Latvian Insurers Association

The life insurance segment in Latvia has increased rapidly in recent years with life endowments as a dominant product. Rapid growth rates are result of the low initial penetration, improved sales effort of insurance companies and middle income segment of population becoming more familiar with life insurance products and willing to purchasing them as a savings instrument. At the end of 2007, life endowment insurance accounted for 71 percent of the total life insurance market and health insurance for 28 percent of the life market. In 2008 life endowments’ market share dropped to 57 percent and health insurance’s market share increased to 41 percent. The decline of the life endowments’ premium income is most probably the result of lower income levels and saving rates, with consumers cutting on any product that can be possibly considered luxurious in times of crisis.

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184 Ibid.
The life insurance market is highly concentrated. In January 2008 there were 10 life insurers active in the Latvian market and the top three accounted for 82 percent of the market. Major players include SEB Dzivibas Apdrosinasana, Sampo Life, ERGO Latvija dziviba and Seesam Life. Some insurers are owned by banks or have agreements with banks for selling their products. Other insurers are owned by major foreign life insurers (ERGO, Seesam Life, etc.) and work with an associated non-life company. There are five branches of foreign insurers and one life insurer works on “a cross-border freedom of services” basis from Austria.185

There has been a significant increase in the number of brokers operating in the market, due mostly to lowered capital requirement. Insurance brokers are registered and regulated under the Activities of Insurance and Reinsurance Intermediaries Law. Brokers can be natural persons or commercial companies but only responsible persons may be directly involved in insurance and reinsurance mediation. A prerequisite for registration is that the applicant must demonstrate sufficient education and experience. There is no direct propriety test within the Law. Recently the capital requirement for broking operations was substantially reduced from the LVL equivalent of Euros 50,000 to LVL 2,000, which is directly related to the increase in the number of brokers operating in the insurance market. This regulatory change made the broker segment more vulnerable to abuse and fraud. In 2009 the FCMC increased the capital requirement for broking operations up to the LVL equivalent of Euros 15,000.

Both tied and free agents are similarly registered under the Law. Applicants are required to satisfy the FCMC’s fitness and propriety requirements. The fitness requirement for agents is less strict than the requirement for brokers, but the propriety requirements are the same. FCMC publishes a register of free agents on its website. Section 21 of the Law requires a register of tied agents to be maintained on the website of the insurance company to which they are tied.

Legal Framework and Institutional Arrangements

The followings are the key laws governing consumer protection in the insurance sector:

- Insurance Contract Law;
- Law on Insurance Companies and Supervision thereof;
- Activities of Insurance and Reinsurance Intermediaries Law;
- Personal Data Protection Law;
- Recommendation for the Formulation of Procedures for Effective Out-of-court Settlement of Consumer Disputes with Insurer regarding the Payment of Insurance Indemnities, FCMC Decision No. 298 (December 2003)

The Financial and Capital Market Commission (FCMC) is a consolidated regulator that has the responsibility for supervising the banking, insurance, securities and private pension sectors of the financial markets. The FCMC acts primarily as a prudential regulator, although it engages in some market conduct regulation as well. The Activities of Insurance and Reinsurance Intermediaries Law requires FCMC to provide opinions to customers regarding complaints relating to violations of the Law. While the Law gives the FCMC a role in consumer complaints, the role is not extended to analyzing complaints, disputes and inquiries specifically.

The Consumer Rights Protection Centre (CRPC) is a direct administration institution supervised by the Ministry of Economics. The Activities of Insurance and Reinsurance Intermediaries Law allows consumers to refer complaints to the CRPC.

The Latvian Insurers Association is the only association to which both life and non-life companies are eligible to join. There is only one company which is not a member of the association. This company is a recent entrant into the Latvian market and has been offered membership. In 2005 the Latvian Insurers Association created the Ombudsman Office to handle complaints against its members. The scope of activities of the Ombudsman Office seems to be relatively limited, covering disputes concerning property and motor vehicle claims (these classes account for the majority of premium income in the non-life market segment) and matters concerning the admissibility of claims and the assessment of the quantum of those claims.

The Latvian Insurance Brokers Association represents 36 broking firms, which cover fifty percent of the market. The association plays a pivotal role in setting and testing the educational requirements for brokers under Section 42 of the Law. The association is lobbying the Government to raise the capital requirement for entry into the industry to a minimum of LVL 15,000.

Key Recommendations

The key recommendations regarding consumer protection in the insurance sector include:

- The law should require insurers specifically to explain to consumers the main rights, duties and obligations of both parties before an insurance contract is concluded.
- The Latvian Insurers Association in conjunction with the FCMC and the CRPC should ensure that a principles-based code of conduct is developed for all participants in the industry and the code is adopted by all industry participants on a mandatory basis.
- The law should be revised to ensure that where consumers are required by merchants or credit providers to insure with a particular company adequate disclosure is made to the consumer. The disclosure should include the relationship between the credit provider or
merchant and the selected insurance provider, the benefits which the merchant or credit provider will derive from the arrangement and a comparison of the costs to the consumer with the costs of a number of other alternatives.

- The Activities of Insurance and Reinsurance Intermediaries Law should be reviewed to ensure that persons cannot act simultaneously as broker and agent. The Law should also require mandatory disclosure of commissions payable to intermediaries in relation to single premium investment products.
- The Law should be reviewed to ensure that the sanctions which may be exercised by the FCMC for violations of the Law are adequate in financial terms, and to allow the FCMC to remove the registration of persons who breach the Law.
- The Law should ensure that intermediaries and insurance undertakings are legally responsible for any false and misleading statement they make in their advertising materials.
- The Law should specify a minimum period during which the intermediaries are required to retain the information provided by the insured, the analysis of the information performed by the intermediary and the recommendation offered by the intermediary.
- FCMC should consider if the cooling-off period is effective where the time between the signing of the contract and the effective date of the contract is less than 15 days because it appears to make the fifteen day notice requirement impossible to achieve.
- The Latvian Insurers Association should prepare Key Facts Statements in plain language for each class of life and non-life insurance products. The association should agree on the content of the statements with the FCMC and the CRPC.
- The Insurance Contract Law should be reviewed to ensure that consumers who hold traditional savings or investment products receive an annual statement of their products and have the right to require statements at more frequent intervals. The Law should also ensure that consumers have available mechanisms for resolving disputes about the accuracy of such statements.
- Insurance undertakings should have in place procedures by which the insurer examines and responds to consumer complaints.
- The FCMC, industry associations and consumer NGOs should increase their role in furthering consumer understanding and knowledge of the insurance market.
### Good Practices: Insurance Sector

<table>
<thead>
<tr>
<th>SECTION A</th>
<th>CONSUMER PROTECTION INSTITUTIONS</th>
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<tbody>
<tr>
<td>Good Practice A.1</td>
<td>Consumer Protection Regime</td>
</tr>
<tr>
<td></td>
<td><strong>The law should provide for clear rules on consumer protection in the area of insurance and there should be adequate institutional arrangements for the implementation and enforcement of consumer protection rules.</strong></td>
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<tr>
<td></td>
<td><strong>a.</strong> There should be specific legal provisions in the law, which create an effective regime for the protection of consumers of insurance services.</td>
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<tr>
<td></td>
<td><strong>b.</strong> There should be either a general consumer agency or a specialized agency responsible for implementing, overseeing and enforcing consumer protection, as well as collecting and analyzing data (including complaints, disputes and inquiries).</td>
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<td></td>
<td><strong>c.</strong> The rules should prioritize a role for the private sector, including voluntary consumer protection organizations and self-regulatory organizations.</td>
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</table>

| Description | Article 3 of the Insurance Contract Law establishes the procedures that insurers have to follow in relation to the resolution of disputes: (i) disputes are to be settled in accordance with the procedures prescribed by the laws and other regulatory enactments, (ii) the parties may agree to resolve disputes by an arbitration court, (iii) the insurer has to notify the insurant of the out-of-court dispute and complaint settlement procedures prior to entering into the contract. In December 2003 the Financial and Capital Market Commission (FCMC) issued the Recommendation for the Formulation of Procedures for Effective Out-of-court Settlement of Consumer Disputes with Insurer regarding the Payment of Insurance Indemnities (Decision No. 298). The purport of this document is to establish an independent Ombudsman. |
| Description | While the above provisions are general, paradoxically the provisions in relation to intermediaries are more specific. Section 29 of the Activities of Insurance and Reinsurance Intermediaries Law creates a duty on insurance intermediaries to ensure the establishment of effective procedures for the examination of consumer complaints which must be available at the place of insurance mediation and must be publicized on the intermediaries’ websites (where such websites exist). The Law also creates an obligation on intermediaries to respond to complaints within one month or such other time that the intermediary can justify, provided that it notifies the insurant (Section 29, paragraphs 2 and 3). Section 24 (5) requires that the intermediary, prior to entering into a contract with an insured person, provide that person with the procedures by which complaints and disputes between the intermediary and the customer shall be examined out of court. Further, Section 31 requires the FCMC to provide opinions to customers regarding complaints relating to violations of the Law. The same Section authorizes consumers to refer complaints to the Consumer Rights Protection Centre (CRPC). |
| Description | While the legislation gives the FCMC a role in consumer complaints, the role does not extend to analyzing complaints, disputes and inquiries specifically. |
| Description | The legislation does not provide associations or other private sector organizations with a formal role in the enforcement of consumer protection rules. |
| Description | In general, the provisions in the Activities of Insurance and Reinsurance Intermediaries Law are more specific and are preferable to the more general provisions in the Insurance Contract Law. |
| Recommendation | The Insurance Contract Law needs to be reviewed in relation to handling consumer complaints and disputes to mirror the requirements of the Activities of Insurance and Reinsurance Intermediaries Law. |
The provisions of both laws should be reviewed to expand the role of the FCMC by requiring it to collect and analyze data on complaints, disputes and inquiries. Both laws need to be reviewed to provide the associations and other private sector organizations (where relevant) with formal roles in consumer protection.

**Good Practice A.2 Contracts**

There should be a specialized insurance contracts section in the general insurance or contracts law, or ideally a separate Insurance Contracts Act. This should specify the information exchange and disclosure requirements specific to the insurance sector, the basic rights of the insurer and policyholder and allow for any asymmetries of negotiating power or access to information.

**Description**

The Latvian insurance regime is divided between three Acts of Parliament – the Insurance Contract Law, the Law on Insurance Companies and Supervision thereof, and the Activities of Insurance and Reinsurance Intermediaries Law. The Insurance Contract Law is relevant here. The Law requires a formal written contract between the parties before the contract is deemed to be concluded (Article 7), and specifies some general information that must be included in the contract such as start and finish dates, sum insured, premiums and mode of payment, duties of the parties, dispute resolution procedures and consequences of not observing those duties (Article 6(2)). The Law imposes a specific duty on the applicant for insurance to make truthful disclosures of all relevant information that the insurer needs to conclude the contract. Acts of bad faith or gross negligence performed by the insurant render the contract void (Article 8). The insured has a duty to inform the insurer if there is a significant increase in the likelihood of the occurrence of the risk event during the currency of the contract (Article 14). Under certain circumstances, the insurer can renegotiate the contract where there has been a significant increase in the aforementioned likelihood (Article 16). The Law gives the insurer the right to cancel the contract and receive a prorated refund of his or her premiums (Article 27). The Law creates an obligation on the insurant to mitigate the insurer’s losses in the event of the occurrence of an event that is the subject of the insurance. (Article 21). Where the insurer fails through negligence to mitigate the losses, the insurer has the right to reduce the payout by a maximum of 50 percent. (Article 22(2)).

The Law gives the insurer the right to void contracts that have been made on the basis of negligence or fraud (Articles 8 and 9). The insurer is obliged to pay claims where the contract has been concluded properly and the premiums paid (Article 24). The Law imposes a maximum time of one month from the date of receiving a claim request in which the insurer itself may request any such further information as it seeks. In normal circumstances the insurer has a further one month to decide on the claim but may extend that time to six months, if it has grounds that justify the extension, subject to advising the insurant in writing and including the justification. (Article 24).

These are generally accepted rights and obligations for both parties.

The Law requires that the contract be evidenced in writing and written in the official language (unless otherwise requested by the applicant) (Article 6-1) and in clear, understandable language. However the Law does not require the insurer to explain to the insurant the terms and conditions of the contract.

Discussions with the FCMC and a review of its website showed an increasing number of complaints to the regulator. The FCMC generally handles complaints that are directed as to whether a particular provision or practice offends the law. It is understood that a large number of these complaints involve insurers not observing the time limits imposed on them by Article 24.

**Recommendation**

Given the particularly technical nature of the insurance contracts and the associated obligations of insured parties (especially the obligations to notify changes in risk characteristics and to mitigate insurer’s losses), as well as the asymmetry of information,
the law should explicitly require insurers to explain to applicants the main rights, duties and obligations of both parties before the contract is concluded.

<table>
<thead>
<tr>
<th>Good Practice A.3</th>
<th>Codes of Conduct for Insurers</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. The law should explicitly require insurers to explain to applicants the main rights, duties and obligations of both parties before the contract is concluded.</td>
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<table>
<thead>
<tr>
<th>Description</th>
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<tbody>
<tr>
<td>There is currently no requirement within the Insurance Contract Law or the Law on Insurance Companies and the Supervision Thereof for companies to have a code of conduct. However, the Activities of Insurance and Reinsurance Intermediaries Law determines the role of associations in the accreditation of brokers and agents. An association which can accredit these parties must have a code of ethics, for agents and brokers respectively.</td>
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</table>

The Latvian Insurers Association does not have a formal code of conduct but has a number of rules of membership which cover some of the elements expected to be found in a code. Members of the association and companies that have applied to join the association must agree to abide by the terms of the rules of the association. Notwithstanding this and the occasions on which companies have breached the association rules, including those which pertain to the elements of a good code, companies are neither disciplined by the association members nor expelled from the association. |

There is no requirement that the companies display any information about their codes of conduct imposed either under the legislation or under the rules of the association. |

The membership of the association covers all but one of the insurers in both life and non-life segments and represents companies which collectively account for more than 99 percent of the gross written premium in the market. The unrepresented company is Nordica Insurance which is a recent entrant into the Latvian market and has already been invited to become a member of the association. The response to the invitation is awaiting approval from the Head Office. |

The Latvian Insurance Brokers Association (which represents 35 broker companies) has developed a code of conduct which is mandatory for all its members. The code appears to be extensive and comprehensive. Copies of the code are available on the websites of the brokers and the association. The unrepresented brokers do not have any obligations in this respect. |

<table>
<thead>
<tr>
<th>Recommendation</th>
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<tbody>
<tr>
<td>It is recommended that the Latvian Insurers Association in conjunction with the FCMC and the CRPC ensure that a principles-based code of conduct is developed for all participants in the industry and adopted by all industry participants on a mandatory basis.</td>
</tr>
</tbody>
</table>

Each participating insurance company should be required to advise consumers and potential consumers of the existence and content of the code and display the code prominently in all its offices. The CRPC should monitor compliance with the code and make comments about the level of compliance in its annual reports. |

The mandatory code should be based on good business conduct and should be supplemented by a voluntary code of conduct developed by the Association and its members. The members should agree to adopt this code voluntarily. The voluntary code |
should be similarly conveyed to consumers and potential consumers. The CRPC should monitor the level of compliance with the voluntary code and comment on the level of compliance with it in addition to the mandatory code.

<table>
<thead>
<tr>
<th>Good Practice A.4</th>
<th>Other Institutional Arrangements</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. There should be a balance between prudential supervision and consumer protection.</td>
<td></td>
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<tr>
<td>b. The judicial system should provide credibility to the enforcement of the rules on financial consumer protection.</td>
<td></td>
</tr>
<tr>
<td>c. The media and consumer associations should play an active role in promoting financial consumer protection.</td>
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</table>

**Description**

FCMC is the prudential regulator for the insurance industry. It has a limited role in consumer protection. The role extends to receiving complaints and investigating those complaints against the statutory provisions within the three insurance laws that it administers. Where there is a violation of these provisions, the FCMC may issue sanctions against the insurer. The financial sanctions are for amounts up to LVL 10,000. The FCMC may also withdraw registrations and authorizations for substantial breaches.

Where consumer complaints do not involve breaches of the three insurance laws but may relate to misunderstandings, unfair treatment or alleged misrepresentation, they are referred to the CRPC.

The role of the FCMC is very limited in relation to the treatment of consumer complaints and is heavily inclined towards prudential supervision.

Insurance complaints can be referred to the CRPC and/or the Insurance Ombudsman. Where one party is dissatisfied with the outcomes of these processes, it may refer the determination on appeal to the Courts. It is reported that resolution of matters through the Courts is costly, lengthy and frequently uncertain.

FCMC does not have a statutory role in educating consumers about consumer rights issues. The Latvian Insurers Association does liaise frequently with the press and does advertise on behalf of the industry from time to time. These activities are more directed at promoting the interests of the industry rather than educating consumers about consumer protection issues.

**Recommendation**

The media and the industry associations should be encouraged to promote consumer awareness of issues relating to consumer protection.

<table>
<thead>
<tr>
<th>Good Practice A.5</th>
<th>Linked Products and Bundling Clauses</th>
</tr>
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<tbody>
<tr>
<td>Whenever an insurer contracts with a merchant or credit grantor (including banks and leasing companies) as a distribution channel for its contracts, no bundling (including enforcing adhesion to what is legally a single contract), tying or other exclusionary dealings should take place without the consumer being advised and able to opt out</td>
<td></td>
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</tbody>
</table>

**Description**

There are no provisions within any of the laws that regulate the insurance industry which prohibit the practice of requiring consumers to insure with particular insurance companies or to use particular brokers or agents.

Intermediaries have a general obligation under Chapter V of the Activities of Insurance and Reinsurance Intermediaries Law to act as an “honest and careful proprietor” and to act with appropriate professionalism and care.

In practice, where a credit provider or merchant requires the consumer to take out particular insurance, the consumer will be presented with a list of suitable insurance companies, generally not less than four, from which to choose.
| Recommendation | The Law should be revised to ensure that where consumers are required by merchants or credit providers to insure with a particular company adequate disclosure is made to the consumer. The disclosure should include the relationship between the credit provider or merchant and the selected insurance provider, the benefits which the merchant or credit provider will derive from the arrangement and a comparison of the costs to the consumer with the costs of a number of other alternatives. |
| SECTION B | DISCLOSURE & SALES PRACTICES |
| Good Practice B.1 | Sales Practices |
| a. | Insurers should be held responsible for product-related information provided to consumers by their agents (i.e. those intermediaries acting for the insurer). |
| b. | Consumers should be made aware of whether the intermediary selling them an insurance contract (known as a policy) is acting for them or for the insurer (i.e. in the latter case they have an agency agreement with the insurer). |
| c. | If the intermediary is a broker (i.e. acting on behalf of the consumer) then the consumer should be advised at the time of initial contact with the intermediary if commission will be paid by the underwriting insurer. The consumer should have the right to require disclosure of the commission and other costs paid to an intermediary for long term savings contracts. The consumer should always be advised of the amount of commission paid on single premium investment contracts. |
| d. | An intermediary should not be allowed to identically fill broking and agency roles for a given general class of insurance (i.e. life and disability, health, general insurance, credit insurance). |
| e. | Sanctions, including meaningful fines and, in the case of intermediaries, loss of license, should apply for breach of any of the above provisions. |
| Description | Chapter V of the Activities of Insurance and Reinsurance Intermediaries Law concerns the relationship between the intermediaries and their customers. Section 23(1) requires the intermediary to act as an “honest and careful proprietor” and to ensure that the customer is dealt with employing “appropriate professionalism and care”. Section 23 also provides that intermediaries cannot enter into contracts with customers that violate those basic tenets (paragraph 2) and provides that losses caused through violations of these tenets are recoverable by the customer (paragraph 3). |
| | Section 24 requires the intermediaries to disclose the following information to consumers prior to entering into or amending an insurance contract: (i) the name, address and contact details of the intermediary; (ii) where the intermediary is registered; (iii) the interests (if any) of the intermediary in any insurance undertaking; (iv) the out-of-court procedures for the handling of complaints and disputes. Section 24 also requires the intermediary to disclose the basis on which an offer is being prepared and whether it is contractually bound to one or a number of insurance undertakings. The intermediary is required at the request of the customer to disclose the remuneration it will receive for a concrete insurance contract. |
| | Where any of the information required is provided only on the basis of a request from the customer, the intermediary has a duty to advise the customer that he or she is entitled to request such information (Section 24(4)). |
| | The information that must be provided under the Law is sufficient to enable the consumer to determine whether the intermediary is acting as a broker or agent. |
| | There are no specific provisions that would prohibit an intermediary from acting as broker and agent in relation to the one product. These terms are not defined within Section 2 of the Law so as to be mutually exclusive. |
Section 41 of the Law provides that the FCMC “has the right to request that an insurance and reinsurance intermediary eliminate determined violations of this Law and carry out the necessary measures for the prevention of such violations”. Section 18 of the Law provides for removal from office of persons directly involved in mediation activities “if it is determined that he or she has caused a situation that may endanger the interests of customers as well as not complying with the requirements specified by the Law”.

With the exception of the foregoing, the sanctions for non-compliance with the disclosure requirements of this Law are not specified.

The foregoing provisions relate to intermediaries as defined under Section 2 of the Activities of Insurance and Reinsurance Intermediaries Law. There do not appear to be any such requirements that are applicable to employees of insurance companies who do not fit within the definition of intermediaries.

**Recommendation**
The Activities of Insurance and Reinsurance Intermediaries Law should be reviewed to ensure that persons cannot act simultaneously as broker and agent.

The Law, which currently permits consumers to request details of commissions payable to the intermediaries in relation to all classes of insurance, should be reviewed to achieve the mandatory disclosure of commissions payable of single premium investment products.

The Law should be reviewed to ensure that the sanctions which may be exercised by the FCMC for violations of the Law are adequate in financial terms and allow the FCMC to remove the registration, on its own volition, of persons who breach the Law.

The obligations created on intermediaries under the Activities of Insurance and Reinsurance Intermediaries Law should be extended to employees of insurance companies who are not within the definition of intermediaries.

### Good Practice B.2
**Advertising and Sales Materials**

- **a.** Insurers should make sure that their advertising and sales materials and procedures do not mislead customers. Regulatory limits should be placed on investment returns used in life insurance value projections.
- **b.** Insurers should be legally responsible for all statements made in marketing and sales materials they produce related to their products.
- **c.** All marketing and sales materials should be easy to read and easy to understand by the average person.

**Description**
The Law on Insurance Companies and the Supervision thereof is relevant to the manner in which insurers can advertise. Article 7(2)(2) specifically prohibits an insurance undertaking “disseminating false and misleading advertising on its activities”. The FCMC does not routinely review the compliance of the industry with this provision except where a complaint may be made against an undertaking.

The Law does not contain any specific provisions that render an insurance undertaking responsible for statements made in its advertising materials.

There do not appear to be similar provisions in the Activities of Insurance and Reinsurance Intermediaries Law that governs the activities of brokers, agents and tied agents. These parties can be commercial companies which themselves advertise. However they are bound to follow the Code of Ethics of their respective associations, where they are members of the association.

A review of some of the advertising material revealed that it tends to be quite complex and lengthy and would benefit from the inclusion of key facts statements referred to later in this section.

**Recommendation**
The Activities of Insurance and Reinsurance Intermediaries Law should be reviewed to ensure that intermediaries are not permitted to advertise in a false and misleading fashion and to ensure that intermediaries that do so are legally responsible for any statements they
make.

The Law on Insurance Companies and the Supervision Thereof should be reviewed to ensure that there are specific provisions that ensure insurance undertakings are legally responsible for any false and misleading statements they make in their advertising materials.

The FCMC should routinely review the advertising material of insurance companies as part of its on-site review processes to ensure that companies are not advertising in a misleading or false manner. As part of the routine review, the FCMC should consider whether the information provided is easy to comprehend.

**Good Practice B.3 Know Your Customer**

The sales intermediary or officer should be required to obtain sufficient information about the consumer to ensure an appropriate product is offered. Formal ‘fact finds’ should be specified for long term savings and investment products and should be retained and available for inspection for a reasonable number of years.

**Description**

The Activities of Insurance and Reinsurance Intermediaries Law contains a specific know your customer provision. Section 25 provides that “prior to entering a contract, an insurance intermediary shall ascertain the requirements and needs of a customer on the basis of the information provided by the customer, as well as the reasons, which are the basis for consultations provided to the customer regarding the relevant insurance service. The insurance intermediary shall prepare such information in accordance with the complexity of the offered insurance contract.” These provisions apply to insurance brokers, agents and tied agents.

There do not appear to be similar provisions in the Insurance Contract Law or the Law on Insurance Companies and the Supervision thereof.

As a consequence it appears that brokers, agents and tied agents have a specific legal obligation to know their customer but that obligation is not extended to insurance companies and the employees of those companies.

The Law does not differentiate the class of insurance to which the "know your customer” obligations apply other than the reference to the preparation of information that is in accordance with the complexity of the offered insurance contract.

There are no provisions in the Law pertaining to how the "know your customer” exercise is to be undertaken or evidenced. There are no provisions governing the minimum time frames during which records (if any) are to be maintained.

**Recommendation**

The Activities of Insurance and Reinsurance Intermediaries Law should be reviewed to provide more fully the mode in which insurance intermediaries meet their obligations under Section 25. The Law should specify a minimum period during which the intermediaries are required to retain the information provided by the insured, the analysis of the information performed by the intermediary and the recommendation offered by the intermediary.

The Law on Insurance Companies and the Supervision Thereof should be reviewed to mirror the requirements of the Intermediaries Law (as reviewed above).

**Good Practice B.4 Cooling-off Period**

There should be a reasonable cooling-off period associated with any traditional investment or long term life savings contract, after the policy information is delivered, to deal with possible high pressure selling and mis-selling.

**Description**

Both life and non-life insurance are regulated under the Insurance Contract Law. Article 27(1) of the Law provides that “the insurer and the policyholder may terminate the policy in the period between the date the policy is concluded and the date the contract takes effect.
The other party shall be notified of such termination not later than *15 days before the contract takes effect.* Article 6 provides that the contract shall start on the date agreed between the parties in the contract. However, at the same time Article 27 (3) states that the policyholder “has the right to terminate the individual life insurance contract within a *15-day period as from the date of concluding the contract*” (this provision is only applicable to life contracts for 6 months or longer).

The effect of these provisions appears that if a person seeking insurance agrees for the contract to start within 15 days (e.g. 10 days) of the signing of the contract, the person might not be able to execute the “cooling off period” (because it is not possible for this person to meet with the requirement of giving at least 15 days notice before the contract commences).

This appears to be inconsistent with Article 45 of EU Directive 2002/83/EC on Life Assurance, which states that a cooling-off period of between 14-30 days should be given for life insurance offerings.

<table>
<thead>
<tr>
<th>Recommendation</th>
<th>The existence of a statutory cooling-off period under Article 27 of the Insurance Contract Law is acknowledged. However there appears to be an anomaly in the wording of this article. The article requires a party wishing to cool off to give at least a 15-day notice before the commencement of the contract (that is between the signing of the contract and the effective date of the contract). FCMC should consider if the cooling-off period is effective where the time between the signing of the contract and the effective date of the contract is less than 15 days because it appears to make the fifteen day notice requirement impossible to achieve.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Good Practice B.5</td>
<td><strong>Key Facts Document</strong> A Key Facts Document should be attached to all sales and contractual documents, disclosing the key factors of the insurance product or services in large print.</td>
</tr>
</tbody>
</table>
| Description | Article 6 (2) of the Insurance Contract Law provides the minimum matters that must be addressed with the terms and conditions of the insurance contract.  

Article 2 permits the insurer to seek such information as it deems necessary from the applicant party. Otherwise, the Law is silent on the disclosures that an insurer must make to the insured and in what form.  

In the insurance sector, plain disclosure of the obligations of the insured is especially important because of the insured's obligations to notify the insurer during the currency of the contract of any facts that may increase the insurer's risk and to mitigate the insurer's loss if an insured event occurs. |
| Recommendation | The Latvian Insurers Association in concert with its members should prepare a key facts statement in plain language for each class of both life and non-life insurance products offered. The association should agree on the content of the statements with the FCMC and the CRPC. Insurance companies, brokers and agents should ensure that a key facts statement forms part of the information given to applicants when an offer of insurance is made and when contracts for insurance are finalized. |
| Good Practice B.6 | **Professional Competence**  

a. Sales personnel and intermediaries selling and advising on insurance contracts should have sufficient qualifications and competence, depending on the complexities of the products they sell.  

b. Educational requirements for intermediaries selling long-term savings and investment insurance products should be specified, or at least approved, by the regulator or supervisor. |
| Description | The selling of insurance products is regulated under the Activities of Insurance and Reinsurance Intermediaries Law. The Law applies to agents, tied agents and brokers
(collectively referred to as "insurance intermediaries"). The Law does not differentiate between parties selling life and non-life insurance products. The Law does not apply to a very limited number of parties, principally those who arrange short-term, non-life insurance with small premiums as part of their normal professional activities (Section 7).

Each intermediary shall either be a responsible person or shall employ a responsible person. A responsible person is defined in Section 1 as a self-employed person or a member of the executive body of an intermediary who "is responsible for insurance or reinsurance intermediation".

The requirements for brokers are provided in Section 17 (1). The broker and responsible person are required to be at least 21 years of age, to have attained appropriate higher education, to be proficient in the official language, to have acquired the knowledge necessary for the performance of the task and to have had at least three years of appropriate experience. Both the knowledge and experience criteria need to be recognized by a professional body of insurance and reinsurance intermediaries.

The requirements for agents are found in Section 17(2). The principal differences are: the minimum age is reduced to 18, the minimum work experience is reduced to one year, and the minimum education level is secondary education. The minimum work experience is not applicable to employees of a registered insurance agent.

The situation for tied agents mirrors the requirements for agents except there is no minimum work experience required. Section 20(3) provides that where an insurance company has tied agents, it is responsible for "the training of the responsible person of a tied insurance agent and employees directly involved in insurance mediation, in order to provide the necessary knowledge regarding the insurance service, which is distributed within the framework of insurance mediation".

The role of the professional bodies is specified in the definitions of Section 1(12) and (13), which refer to those bodies that have received a permit from FCMC to provide the statements required under the Law regarding knowledge and work experience requirements to perform insurance intermediation.

The situation regarding sales personnel employed by insurance companies and who are not agents is not clear.

| Recommendation | The Law should be reviewed to clarify the requirements of sales personnel employed within insurance companies. |
| Good Practice B.7 | Regulatory Status Disclosure |
| | a. In all of its advertising, whether by print, television, radio or otherwise, an insurer should disclose: (a) that it is regulated and (b) the name and address of the regulator. |
| | b. All insurance intermediaries should be licensed and proof of licensing should be readily available to the general public, including through the internet. |
| Description | All insurance companies and reinsurance companies are required to be registered by FCMC under Chapter II of the Law on Insurance Companies and Supervision Thereof. Insurance brokers, agents and tied agents are required to be registered under Chapter 11 of the Activities of Insurance and Reinsurance Intermediaries Law. Prior to entering into a contract, an insurance intermediary is required to disclose the register in which the insurance intermediary is registered and a way in which to verify the registration thereof. This appears to be the only obligation on intermediaries to disclose their regulated status. There are no requirements in either Law that the company or the intermediaries, as the case may be, disclose the fact that they are registered, the name of the supervisor or its address. It appears that in practice the industry and the intermediaries do not disclose this information on their documentation or websites. |
The insurance companies maintain a register of agents which are tied to them as required by the Activities of Insurance and Reinsurance Intermediaries Law.

The FCMC maintains a register of insurance companies, brokers and agents on its website. If a consumer wants to verify that he or she is dealing with a registered undertaking, he or she must be aware of the FCMC website and access the information there, except where a mandated disclosure has been made in relation to intermediaries.

**Recommendation**

The FCMC should require all regulated insurance undertakings and intermediaries to disclose in their advertising material that they are regulated, by which agency and the address of the agency. The name and address of the regulator should also be shown on the websites of each of these parties.

**Good Practice B.8 Disclosure of Financial Situation**

a. The regulator or supervisor should publish annual public reports on the development, health, strength and penetration of the insurance sector either as a special report or as part of the disclosure and accountability requirements under the law governing it.

b. Insurers should be required to disclose their financial information to enable the general public to form an opinion with regards to the financial viability of the institution.

c. If credible claims paying ability ratings are not available, the regulator or supervisor should periodically publish sufficient information on each insurer for an informed commentator or intermediary to form a view of the insurer’s relative financial strength.

**Description**

FCMC publishes an Annual Report which contains references to the insurance industry. The references are limited to some general observations about the industry in aggregate and the FCMC’s activities in its supervision of the industry. The Annual Report also contains some aggregate data about each of the industries that the FCMC supervises. There is not sufficient information for the consumer to make judgments about individual companies but only the state of the industry as a whole.

The FCMC may like to consider the Annual Report of the Insurance Supervisory Commission in Romania, which publishes details of provisions, claims, technical and mathematical reserves, results on technical account and overall result for each insurance company.

FCMC also performs a statistical service each quarter by publishing some general information about the performance of the industry, supplemented with detailed information about key variables such as technical and mathematical reserves. All these statistics are also presented on an industry wide aggregate basis. Again, there is sufficient information for a technically proficient and knowledgeable person to form a view about the state of the industry but not individual entities within the industry. It is doubtful whether persons who do not have proficiency in insurance would be assisted with the information provided.

Insurance companies have an obligation under Chapter VII of the Law on Insurance Companies and the Supervision Thereof to prepare financial accounts in accordance with the Law on Accounting and the FCMC regulations. The Latvian requirements mirror International Financial Reporting Standards. Article 51 of the Law requires the lodgment of reports with the FCMC, however the law is silent on distributing Annual Reports more widely. In practice, companies publish their annual reports on their websites.

The information provided in individual Annual Reports is quite complex and may be difficult to understand for consumers without a technical background in insurance. It would be of assistance to these persons if companies were required by FCMC to add a simplified set of

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186 Available at http://www.csa-isc.ro/eng/
accounts prepared in more general language.

There are no accounting and reporting requirements for intermediaries under the respective Law.

**Recommendation**

The FCMC should consider providing additional details about the performance of individual insurance companies in both its Annual Report and the quarterly statistical services that it provides.

The FCMC should consider requiring insurance undertakings to publish in their Annual Reports simplified financial statements that will allow consumers without a technical background in insurance to make assessments about the financial viability of the companies.

**SECTION C**

**CUSTOMER ACCOUNT HANDLING AND MAINTENANCE**

**Good Practice C.1**  
**Customer Account Handling**

- a. The customer should receive periodic statements of the value of their policy in the case of insurance savings and investment contracts. For life insurance (which covers both risk coverage and investment), the customer should receive statements on the portion of the premium used for risk cover vs. investment.
- b. For traditional savings contracts, this should be provided annually, however, more frequent statements should be produced for investment-linked contracts.
- c. Customers should have a means to dispute the accuracy of the transactions recorded in the statement within a stipulated period of time.
- d. Insurers should be required to disclose the cash value of a traditional savings or investment contract upon demand and within a reasonable time. In addition, a table showing projected cash values should be provided at the time of delivery of the initial contract and at the time of any subsequent adjustments. The customer should be advised of the assumptions made when preparing the projected cash value of the policy. Alternatively, the projection could be prepared with 0% expected return in order to clearly illustrate the effect of fees.
- e. Customers should be provided with renewal notices a reasonable number of days before the renewal date for non-life policies. If an insurer does not wish to renew a contract it should provide a reasonable notice period.
- f. Claims should not be deniable or adjustable if non disclosure is discovered at the time of the claim but is immaterial to the proximate cause of the claim. In such cases, the claim may be adjusted for any premium shortfall or inability to recover reinsurance.
- g. Insurers should have the right to cancel a policy at any time (other than after a claim has occurred – see above) if material non disclosure can be established.

**Description**

Article 54 of the Insurance Contract Law provides that for personal (i.e life, health or physical condition) policies with a term greater than 12 months, the insurer shall notify the insured of gratuities (bonuses) granted at least every twelve months.

This appears to be the only notification requirement within the Law and does not necessarily cover investment linked products.

As there are no formal requirements for the production and delivery of statements within the Law, there are no provisions relating to disputing the accuracy of the statements and the time frames within which to do so.
There are no explicit provisions within the Law that give the insured the right to require the insurer to provide specific information during the currency of the contract of insurance.

There are no specific requirements within the Insurance Contract Law to require the insurer to give the insured notice of the impending expiration of the term of the policy or to issue a renewal notice – industry practice however is that this occurs.

Article 24 of the Law relates to the rights and duties of the insurer after an insured event has occurred. The Law is silent on the right of the insurer to refuse or adjust a claim in the event of a non-disclosure. However, Article 9 (6) provides that if the insured has committed an act of ordinary negligence (including misleading statements) and the insured event occurs before the termination of the contract or its amendment, the insurer is obliged to indemnify the insured but can reduce the claim in such proportion as exists between the actual premium paid and the premium that would have been paid had the misleading statement not been made.

Article 8 provides the insurer with the right to cancel a contract without refunding the premium where bad faith or gross negligence can be established. In the event of ordinary negligence, Article 9 permits the insurer to negotiate with the insured a revised premium. If the insured does not accept the revised premium, the insurer may cancel the contract and refund the premium on a prorata basis. Where the insurer proves that it would not have concluded the contract if the correct disclosures had been made, the insurer can cancel the contract and refund part of the premium on a prorata basis.

**Recommendation**

The Insurance Contract Law should be reviewed with a view to ensuring that persons who hold traditional savings or investment products receive an annual statement of the transactions involving those products and that the persons have the right to require statements at more frequent intervals. The Insurance Contract Law should ensure that the consumer has available a mechanism for resolving disputes and complaints about the accuracy of such statements.

The Law should be reviewed to ensure that insurers are required to notify insured persons about the need to renew policies that are due to expire and to provide a renewal notice to that effect.

The Law should be reviewed to clarify the rights of the insurer to reduce claims where misstatements have been discovered after the risk has occurred, where misstatements have not been caused by negligence or gross negligence.

### SECTION D

**PRIVACY & DATA PROTECTION**

**Good Practice D.1**

*Confidentiality and Security of Customers’ Information*

Customers have a right to expect that their financial transactions are kept confidential. The law should require insurers to guarantee that they protect the confidentiality and security of personal data, against any anticipated threats or hazards to the security or integrity of such information, and against unauthorized access.

**Description**

There are no specific requirements within the insurance legislation relating to the protection of information that is held by insurers, brokers, agents or tied agents. However, these parties are bound by the Personal Data Protection Law and are required to observe that Law.

It is interesting to note that within the Activities of Insurance and Reinsurance Intermediaries Law, a prerequisite for registration of brokers is the lodgment with the FCMC of the procedures in place for the protection of information systems (presumably unauthorized access or usage included). No such provisions exist in the other insurance legislation.
Recommendation | Article 7(2) of the Insurance Companies and Supervision Thereof Act protects the confidentiality of consumer information. Insurers are also bound by the provisions of the Personal Data Protection Law. Moving forward, FCMC needs to ensure that insurers are aware of and comply with any changes in the Personal Data Protection Law.

**SECTION E** | **DISPUTE RESOLUTION MECHANISMS**

**Good Practice E.1** | **Internal Dispute Settlement**

a. The supervisory agency should require an internal avenue for claim and dispute resolution practices by the insurer.
b. Insurers should designate employees to handle retail policyholder complaints.
c. The insurer should inform its customers of the internal procedures on dispute resolution.
d. The regulator or supervisor should oversee whether insurers comply with their internal procedures on consumer protection rules.

**Description**

Dispute resolutions are referred to in the Insurance Contract Law which governs the general rights and obligations of both parties. Article 3 (e) requires that disputes related to insurance contracts be resolved in accordance with the procedures prescribed by laws and other regulatory requirements. There do not appear to be any specific requirements on dispute resolution in the laws and regulations governing insurance. There are no specific requirements in the Law or practices of the regulator that ensure insurers and their intermediaries appoint an internal disputes resolution person or persons. However, the practice is to do so in insurance companies at least. Apart from the general obligations referred to above, the Law does not require the disclosure of an internal dispute resolution mechanism.

In the Activities of Insurance and Reinsurance Intermediaries Law, a prerequisite for registration of brokers is that they must have in place procedures by which the intermediary examines customer complaints. Further, Section 29 of this Law requires an intermediary to ensure that it has effective procedures for the examination of customer complaints and that written information about the procedures is freely available at the office and on the Internet (where relevant). Customers must receive a response to their complaints within one month or such other time that the intermediary can justify, subject to it advising the complainant.

**Recommendation**

The three laws that govern the insurance sector contain provisions that permit insured parties to query information, and provisions that oblige insurers, brokers and agents to have in place procedures for dealing with such queries. It is not clear from the laws and any pronouncements from FCMC whether there is an expectation that each insurer, broker and agent would have in place an internal body or person who is entrusted with resolving disputes between them and the third party complainant. FCMC should consider (if not already done) requiring a formal internal dispute resolution mechanism within the procedures of each insurer, broker and agent.

**Good Practice E.2** | **Formal Dispute SettlementMechanisms**

a. A system should be in place to allow consumers to seek affordable and efficient third-party recourse, which could be an ombudsman or tribunal, in the event the complaint with the insurer is not resolved to their satisfaction in accordance with internal procedures.
b. The role of an ombudsman or equivalent institution vis-à-vis consumer complaints should be made known to the public.
c. The ombudsman or equivalent institution’s impartiality and independence from the appointing authority and industry should be assured.
d. The enforcement mechanism of the decisions of the ombudsman or equivalent institution and binding nature of the decision on banks should be established and publicized.
In 2005 the Latvian Insurers Association created the Ombudsman Office to handle complaints against its members. The Association advised that the office was created at the request of the regulator. The general conditions of the Ombudsman are contained in the FCMC Board Decision of 19 December 2003 Regarding approval of the recommendation for the formulation of procedures for effective out of court settlement of consumer disputes with insurer regarding the payment of insurance indemnities.

The Ombudsman is appointed by the Association for a two year term and is eligible for reappointment at the expiration of the term. The incumbent who has been in office since the inception is a sworn attorney who is employed by a law firm in Riga and was previously employed in the insurance sector – she is reported to have both knowledge of and experience in the sector.

The scope of activities of the Office seems to be relatively limited, related only to disputes concerning property and motor vehicle claims (these classes account for the majority of premium income in the non-life market segment) and to matters concerning the admissibility of claims and the assessment of the quantum of those claims. This limited scope is not contained within the FCMC formulated recommendation but appears to be operative.

When the admissibility of a claim or the quantum of the claim are in dispute, the company involved is required on a good practice basis to advise the customer of his or her access to the CRPC, the Ombudsman or the Courts. On occasion, complaints are lodged in the initial instance with the CRPC, which can refer them to the Ombudsman.

Complaints are lodged initially through the Latvian Insurers Association. The Association requires a small fee from the complainant and a more significant fee (LVL 100 or LVL 150) from the company involved. All complaints are then referred to the Ombudsman Office who determines whether the matter is within the scope of the activities of the Office. Where they are outside the scope, the complaint is returned via the Association and the Ombudsman advises the complainant of the limited jurisdiction of the Office and elaborates the other avenues (the Court or the CRPC).

The payments made by both the complainant and the company are remitted to the Ombudsman where the complaint is within scope, and refunded to the relevant parties where the complaint is not. The Ombudsman is paid on a case by case basis and does not receive a retainer from the Association.

The recommendations of the Ombudsman are not binding on either party and in no way affect the rights of either party in any subsequent legal action, if pursued.

In the first years of operation of the Office, a small number of complaints were being handled (approximately 2 to 3 a year). Since 2008, the number of complaints has escalated to 3 to 5 cases per month. It is reported that many of the complaints being handled involved the quantum of the claim - in an economy where asset prices have fallen sharply. The Association estimates that above 90 percent of the recommendations are adopted by both parties.

The Ombudsman also reports to the regulator on an annual basis. While the regulator’s website refers to complaints handled by the agency, there is no reference to the activities of the Ombudsman.

Details about the availability and the scope of activities of the Ombudsman and applications are on the Latvian Insurers Association website. There do not appear to be details of the activities undertaken and the matters resolved on the website. However, under the recommendation of the FCMC, the Ombudsman is expected to submit an annual report on the disputes examined during the year to individual companies and they are expected to
publish this report on their websites.

There do not appear to be similar dispute resolution bodies for brokers and agents.

Recommendation

The laws should be examined with a view to harmonizing the requirements across the Law on Insurance Companies and the Supervision Thereof and the Activities of Insurance and Reinsurance Intermediaries Law in relation to an external out-of-court settlement procedure.

Formalizing the existing Ombudsman arrangement within the relevant Law needs to be considered.

The Latvian Insurance Brokers Associations should be encouraged to create an Ombudsman similar to the office that relates to insurance undertakings.

**SECTION F**

**GUARANTEE SCHEMES AND INSOLVENCY**

**Good Practice F.1**

*Guarantee Schemes and Insolvency*

a. With the exception of schemes covering mandatory insurances, guarantee schemes are not to be encouraged for insurance because of the opaque nature of the industry and the scope for moral hazard. Strong governance and supervision are better alternatives.

b. Nominal defendant arrangements should be in place for mandatory insurances such as motor third party liability insurance.

c. Assets covering life insurance mathematical reserves and investment contract policy liabilities should be segregated or at the very least earmarked, and long-term policyholders should have preferential access to such assets in the event of a winding-up.

**Description**

The Fund for the Protection of the Insured has been established to protect the interests of the insured in the event of bankruptcy of an insurer. According to Article 93(1) of the Law on Insurance Companies and Supervision Thereof, the resources of the Fund shall be used for the manager’s remuneration, for the cover of expenses relating to organizing insurance indemnity payments, and for insurance indemnity payments (if the policyholder is a natural person) as follows:

1. 100% of the insurance indemnity, but not more than 2 000 lats to one policyholder, for life assurance, excluding the unit linked life insurance;
2. 50% of the insurance indemnity, but not more than 2 000 lats to one policyholder, for the classes of insurance mentioned in Article 12, Clauses 1-3, 8-10, 13 and 18 of this Law.

The Latvian insurance guarantee schemes comply with the EU Directives on Insurance. Only the mandatory schemes are present.

The Law complies with the EU Directive concerning nominal defendant arrangements.

The prudential standards which are applicable to Latvian life insurers are based on the European directives and require the segregation of assets to cover mathematical reserves, providing protection for policyholders in the event of the bankruptcy of the insurer.

**Recommendation**

No recommendation.

**SECTION G**

**CONSUMER EMPOWERMENT**

**Good Practice G.1**

*Information Resources for Consumers*

a. Consumers, especially the most vulnerable, should have access to sufficient resources to enable them to understand the financial products and services available to them.
### Good Practice G.2 Measuring Financial Capability

#### a. Policymakers, industry and advocates should understand the financial capability of various market segments, particularly those most vulnerable to abuse.

#### b. In order to ensure that financial consumer protection, education and information initiatives are proportionate and appropriate, and in order to measure the effectiveness of those initiatives over time, the financial capability of consumers should be measured periodically by way of large-scale market research that gets repeated from time to time.

For these purposes, the term “financial capability of consumers” means the ability to manage money, keep track of finances, plan ahead, choose appropriate financial products and services and stay informed about financial matters.

### Description

There do not appear to be any initiatives to test the levels of consumer understanding about the insurance industry or to increase the level of consumer literacy in relation to the insurance industry and market.

### Recommendation

Any plans to test the level of financial literacy amongst consumers should include an assessment of the extent to which consumers are aware of the need for insurance both as a risk mitigation tool and a long-term savings tool. Any initiatives to increase the levels of financial literacy should contain detailed information about this segment and its products.
Latvia: Consumer Protection in the Pensions Sector

Overview

The pension reform implemented in Latvia in 2001 provided for the creation of Pillar II and Pillar III pension fund managers. The rate of contributions for Pillar II pensions is set in the law at 10 percent. At the point of retirement, participants have a choice of adding the capital in the second pillar to the non-funded pension capital and have the old age pension recalculated, or to use the capital to purchase an annuity from a life assurance company.

The number of participants in the Pillar II scheme has almost doubled in the past 4 years. As of June 2009 there were 1.08 million participants which represented 88.5 percent of the economically active Latvian residents. Fifty eight percent of the participants had joined on a mandatory basis (being persons born after 1 July 1971). The balance represents participants who joined voluntarily.

The net assets of the Pillar II investment plans totaled LVL 464 million by December 2008, an increase of 94 percent over the previous year. As of June 2009 the net assets increased 34 percent relative to December 2008, reaching LVL 621 million. There are 10 fund management companies and these funds collectively offer 27 investment plans.

In aggregate, the investment profile in the second pillar is quite conservative. 40 percent of funds are invested in debt securities, 45 percent in credit institutions and 15 percent in investment certificates with investment funds. The exposure to shares and other fixed income securities represented less than 1 percent. Of the total investments, 70 percent were with Latvian counterparties and more than 90 percent of the balance with European Union states. The average return over all the plans in 2008 was -11.5% reflecting conditions in global financial markets. More aggressive investment plans reported returns of greater than -25%.

<table>
<thead>
<tr>
<th>Table 10: Size of the Pillar II Pension Scheme</th>
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<tbody>
<tr>
<td></td>
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<tr>
<td><strong>2004</strong></td>
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<tr>
<td>Number of participants</td>
</tr>
<tr>
<td>Number of funds</td>
</tr>
<tr>
<td>Number of investment plans</td>
</tr>
<tr>
<td>Assets of investment plans (LVL thousand)</td>
</tr>
</tbody>
</table>

Source: FCMC, Quarterly Reports

The number of participants in the Pillar III scheme represents about 15 percent of Latvia’s economically active population. As of June 2009 there were six private pension funds – five open funds and one closed. As with the Pillar II scheme, private pension funds can offer more than one pension plan. By June 2009, the six pension funds offered 19 different pension plans and had approximately 186,000 members. 65 percent of the members were active (i.e. had made a contribution in the last twelve months) and 25 percent had reached retirement age, had ceased making contributions to the funds and were receiving their entitlements in installments. The balance represented persons who had retained membership but were inactive (i.e. had not made a payment in the last twelve months.)

The assets of the Pillar III pension funds have tripled in less than five years. By June 2009 the assets of Pillar III pension funds reached LVL 86 million. These assets are represented largely by deposits with credit institutions, bonds and fixed interest securities and investment certificates in investment funds. Recent contributions have averaged about LVL 5 million per quarter -more than 60 percent of these contributions are made by employers on behalf of employees.
Table 11: Size of the Pillar III Pension Scheme

<table>
<thead>
<tr>
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<tr>
<td>Number of participants</td>
<td>39,050</td>
<td>67,904</td>
<td>99,596</td>
<td>142,962</td>
<td>178,338</td>
<td>186,298</td>
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<tr>
<td>Number of funds</td>
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<td>6</td>
<td>6</td>
<td>6</td>
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<td>6</td>
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<tr>
<td>Number of investment plans</td>
<td>12</td>
<td>13</td>
<td>15</td>
<td>16</td>
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<td>19</td>
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<tr>
<td>Assets of investment plans (LVL thousand)</td>
<td>27,175</td>
<td>36,806</td>
<td>51,614</td>
<td>69,825</td>
<td>80,876</td>
<td>86,393</td>
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</table>

Source: FCMC, Quarterly Reports

Legal Framework and Institutional Arrangements

The followings are the key laws governing consumer protection in the insurance sector:

- Law on State Funded Pensions
- Law on Private Pension Funds
- Personal Data Protection Law
- Law on the Financial and Capital Market Commission

The arrangements for the provision of Pillar II pensions in Latvia are regulated under the Law on State Funded Pensions. The Law gives the primary ministerial responsibility to the Minister of Welfare.

There is one provider, the State Social Insurance Agency (SSIA), which acts as the sole pension fund management company for Pillar II. The SSIA establishes and maintains the accounts of participants and informs the participants periodically regarding the state of their accounts and any significant changes to the operations of the scheme. SSIA contracts with fund managers to facilitate the management of the funds of the scheme. While the investments are managed through the fund managers appointed by the SSIA, the assets are held by licensed custodians. Fund managers are permitted to offer more than one investment plan, subject to registering a prospectus with the Financial and Capital Market Commission.

The overall scheme is blind in that the participants enter into contracts with the SSIA, which outsources the management of the funds. Thus fund managers are generally unaware of the identities of the persons on whose behalf they are investing the funds. Participants can transfer between investment plans offered by a specific fund manager twice a year and can change fund managers annually. The transfers are arranged generally by the SSIA although participants can deal directly with the fund managers to affect a transfer.

The Financial and Capital Market Commission (FCMC) is a consolidated regulator that has the responsibility for supervising the banking, insurance, securities and private pension sectors of the financial markets. The FCMC acts primarily as a prudential regulator, although it engages in some market conduct regulation as well. The FCMC handles individual consumer issues that involve breaches of the laws that the FCMC administers. The balance of consumer issues is handled by the Consumer Rights Protection Centre.

The Consumer Rights Protection Centre (CRPC) is a direct administration institution supervised by the Ministry of Economics. The CRPC does not have a specific mandate in relation to pension funds. There is no specialized agency responsible for the implementation, oversight and enforcement for consumer protection for the pension industry.

The Association of Private Pension Funds has developed a code of conduct for its members. A copy of the code is on the website of the association but it is generally not publicized within each provider.
Key Recommendations

- The pension laws should be reviewed to recognize a consumer protection agency for the pension sector.
- A specific role for private sector organizations and self regulatory organizations should be recognized in the Law and supported by the Government.
- The law should be reviewed with a view to ensuring the development of a code of conduct for providers of third pillar pension products.
- The laws should provide specifically that the provider is legally responsible for the information that it provides to consumers in its marketing and sales materials.
- Key Facts Statements should be developed by the SSIA and the Pillar III industry associations.
- The law should be revised in order to require SSIA and pension management companies to provide consumers with specific disclosures (e.g. details of investment risk, complaint handling procedures, change of fees).
- The law should provide for know-your-customer rules.
- The Law on Private Pensions should be reviewed to ensure that all consumers have a cooling-off period during which they can cancel a contract entered into with a Pillar III pension fund. The Law should ensure that consumers are made aware of this right.
- The Law on State Funded Pensions should be reviewed to specify the periodicity, contents and style of customer account statements.
- The law should incorporate the manner in which contributors can resolve complaints or disputes against pension fund management companies.
- The government authorities should coordinate to improve consumer awareness on the pension system.
## Good Practices: Pensions Sector

<table>
<thead>
<tr>
<th>SECTION A</th>
<th>CONSUMER PROTECTION INSTITUTIONS</th>
</tr>
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</table>
| **Good Practice A.1** | **Consumer Protection Regime**  
*The legal system should recognize and provide for clear rules on consumer protection in the area of private pensions and there should be adequate institutional arrangements for the implementation and enforcement of consumer protection rules.*

| a. | There should be specific legal provisions in the law which creates an effective regime for the protection of consumers who deal with pension entities. |
| b. | There should be a general consumer agency or specialized agency responsible for the implementation, oversight and enforcement of consumer protection, and data collection and analysis (including complaints, disputes and inquiries). |
| c. | The legal system should provide a role for the private sector, including voluntary consumer protection organizations and self-regulatory organizations. |

### Description

Pension funds are regulated under the Law on State Funded Pensions (Pillar II) and the Law on Private Pension Funds (Pillar III). Neither Law contains effective consumer protection provisions. In practice, two agencies deal with consumer protection issues. The FCMC handles individual consumer issues that involve breaches of the laws that it administers. The balance of consumer issues that does not involve breaches of the laws is handled by the Consumer Rights Protection Centre (CRPC).

The CRPC does not have a specific mandate in relation to pension funds. There is no specialized agency responsible for the implementation, oversight and enforcement for consumer protection for the pension industry. There is a lack of detailed analysis of the complaints, disputes and inquiries specific to the pension sector.

The Law on State Funded Pensions includes provisions relating to the settlement of disputes (Chapter IV Section 15), but their scope is very limited. The Law recognizes the right of natural and legal persons to appeal to the courts decisions taken during the implementation of the funded pension scheme, and establishes that disputes arising due to non-payment of statutory contributions by employers and disputes arising from claims of the State Social Insurance Agency against fund managers should also be taken to court.

There is no dedicated role for the private sector within the pension legislation.

### Recommendation

The pension laws should be reviewed to recognize a consumer protection agency for the pension sector. The responsibilities of the agency should include the collection and analysis of data concerning complaints, disputes and inquiries within the sector.

A specific role for private sector organizations and self-regulatory organizations should be recognized in the law and supported by the Government.

| **Good Practice A.2** | **Other Institutional Arrangements**

| a. | The judicial system should provide credibility to the enforcement of the rules on consumer protection. |
| b. | The media and consumer associations ought to play an active role in promoting consumer protection. |

### Description

The media and consumer associations do not actively cover consumer protection issues regarding the pension industry.
**Recommendation**

The media and the consumer associations should be encouraged to promote consumer awareness of issues relating to consumer protection in the pension sector.

**Good Practice A.3**

**Codes of Conduct for Pension Entities**

- There should be a principles-based code of conduct for pension entities that is devised in consultation with the industry and relevant consumer protection associations, and is monitored and enforced as a last resort by a statutory agency.
- Pension entities should publicize the statutory code to the general public through appropriate means.
- The statutory code should be limited to good business conduct principles. It should be augmented by voluntary codes on matters specific to the product or channel concerned.
- The operation of voluntary codes should be monitored by a statutory agency, and the Annual Report of that agency should comment on the operation of those codes.

**Description**

There are no requirements in either the Law on Private Pension Funds or the Law on State Funded Pensions for the providers to have a code of conduct on a mandatory basis. The only management company in the second pillar fund is the State Social Insurance Agency (SSIA) and, naturally, there is no association. The only other providers in this Pillar are asset management companies that generally do not directly interact with consumers given the blind nature of the scheme.

Although the Law on Private Pension Funds does not require a statutory code of Conduct, the Association of Private Pension Funds has developed a code of conduct for its members. A copy of the code is on the website of the association but it is generally not publicized within each provider. The code is entirely voluntary. It does not appear that the regulator monitors the level of compliance with the code and no information about the level of compliance is available from the regulator or its website.

**Recommendation**

As a first step, the Association should develop a clear and effective mechanism to investigate breaches of the code of conduct, including the possibility that these breaches be publicized. The financial supervisory agency could use information on these breaches as warning signals for further issues to look at. As a further step, the Law on Private Pension Funds should be reviewed with a view to ensuring the development of a statutory code of conduct for providers of third pillar services. The regulator’s authority should then be expanded to include review of compliance with the code by the pension providers, and disclosure of compliance in its annual reports. The FCMC could include the monitoring of compliance as one of the “thematic inspections” contemplated under Article 28(4) of the Law.

The Law should also encourage the development of additional codes of conduct by individual providers that are specific to the products and channels that are relevant to that provider.

**SECTION B**

**DISCLOSURE AND SALES PRACTICES**

**Good Practice B.1**

**General Practices**

- There should be principles of disclosure that cover the consumer’s relationship with the pension entity in all three stages of such relationships: pre-sale, point of sale, and post-sale.
- There should be clear rules on solicitation and issuance of pension products.
- The information available and provided to the consumer should clearly inform the consumer of the choice of accounts, products and services.
- The pension entity should be legally responsible for all statements made in marketing and sales materials related to their products.
| Description | According to the Law on State Pension Funds, the SSIA is the administrator of the second pillar pension scheme. The SSIA appoints fund managers to invest part of the funds of the scheme. The fund managers need to be authorized by the FCMC. Section 11(4) of the Law on State Pension Funds requires fund managers to develop one or several plans for the investment of funds, which are presented in a prospectus of the relevant investment plan. The prospectus (prospectuses) of an investment plan is an integral part of the contract entered into between the SSIA and the manager of funds. The manager of funds is entitled to perform the management of funds in conformity with an investment plan only following the registration of the prospectus of the relevant investment plan with the FCMC. If the prospectus of an investment plan does not conform to the requirements specified in regulatory enactments, the FCMC shall reject its registration.

The nature of the Pillar II pension fund scheme is that it is mandatory and the scheme operates as a monopoly. There are no rules on solicitation within the legislation.

The Law is silent on what occurs at the point of sale other than the conclusion of a contract.

There are no specific provisions within the legislation that render the provider responsible for statements made in advertising, marketing or sales materials.

During the currency of the contract, the SSIA is required to issue statements to contributors "periodically". However the Law neither defines what it means by "periodic" nor regulates the content of the statements. For greater discussion on the statements, please see Good Practice C.1.

The requirements under the Law on Private Pension Funds are similar. The difference is that the pension fund management companies are required to issue statements to contributors at least annually (see Good Practice C.1).

The Law is silent on what occurs at the point of sale other than the conclusion of a contract. However the May 2009 amendments to the Law included some minimum requirements of information that pension fund management companies should provide to potential contributors, such as the amount of deductions, conditions of membership termination, and retirement benefits arrangements (Article 10(8)).

There are no specific provisions within the legislation that render the provider responsible for statements made in advertising, marketing or sales materials.

| Recommendation | Both laws should be reviewed with a view to ensuring that there is sufficient information given to potential contributors before the contract is concluded. At the time of conclusion of the contract, each Law should require that the SSIA or the fund manager, where relevant, explain the terms and conditions of the contract to the applicant (without the need of an applicant’s request).

Both laws should provide specifically that the provider is legally responsible for the information that it provides to consumers in its marketing and sales materials.

| Good Practice B.2 | **Advertising and Sales Materials**
| | a. Pension entities should ensure that their advertising and sales materials and procedures do not mislead the customers.
| | b. All marketing and sales materials should be easy to read and understand by the average person.

| Description | In relation to the Pillar II scheme, there are no advertising requirements for the SSIA. However, the Law on State Funded Pensions (Section 11-1) contains advertising requirements in relation to the pension fund managers:

(i) Any advertising of the pension fund managers may occur only in conformity with the
prospectus of the investment plan registered with the FCMC;
(ii) The advertising of the investment plan shall indicate:
    a) the name of the investment plan;
    b) the name and legal address of the management company;
    c) the name of the custodian;
    d) the place of submission of the prospectus of the investment plan; and
    e) a notice that the current yield does not guarantee a similar yield in the future (if
    the advertisement mentions the yield of the investment plan).
(iii) The advertising of the investment plan shall in no way guarantee a profit or a specific
level of yield.

There are no requirements concerning the readability of the advertising. There appear to be no sanctions within the legislation that specifically covers breaches of Section 11.

In relation to the Pillar III scheme, Article 9-1 of the Law on Private Pension Funds contains similar provisions:

(i) Any advertising of pension fund operations and services shall only be carried out in
accordance with a pension scheme registered with the FCMC. Where a pension fund’s
defined contribution scheme that does not guarantee an investment performance is
advertised, a profit or a definite level of investment performance shall not be guaranteed.
Where investment performance of a pension scheme is indicated, a statement should made
to precise that the historic investment performance is not a guarantee of a similar
investment performance in the future.
(ii) The advertisement of a pension scheme shall indicate the following:
    a) the name of the pension scheme;
    b) the firm name and legal address of the pension fund;
    c) the name and legal address of the pension scheme’s asset manager;
    d) the name and legal address of the pension scheme’s custodian;
    e) the place where information on the pension scheme and its investment policy is
available.

Again there are neither requirements concerning readability of advertising nor sanctions for
breaches of the provisions on advertising.

Recommendation

Both laws should be reviewed to introduce realistic penalties for breaches of the advertising
requirements (under Section 11 of the Law on State Funded Pensions and Article 9 of the
Law on Private Pension Funds) and to ensure that the information provided by the pension
funds through advertising is readable for all contributors.

Good Practice B.3

Key Facts Document

A Key Facts Document should be presented by the pension entity before the
employee signs a contract, disclosing the key factors of the pension scheme and
its services.

Description

There are no requirements in either the Law on State Funded Pension Funds or the Law on
Private Pension Funds for the funds to present prospective members with key facts
statements and in practice a key facts statement is not prepared.

Recommendation

In relation to Pillar II, the SSIA should prepare a key facts statement that covers amongst
other things, the objectives of the scheme, how it operates, the ability of members to
transfer between options within the fund manager twice a year and the fund manager
annually. This key facts statement should be presented to members when they initially
contract with the SSIA and when they are considering switching investment options or fund
managers.

With regard to Pillar Three, the industry association should prepare a key facts statement
which is reviewed and commented on by the FCMC. This key facts statement should cover,
in plain terms, amongst other things, the fees and deductions, methods and procedures for
payment, the ability of members to transfer without fee and at will between funds and investment options, the fact that contributions are preserved until retirement age, how the member can have complaints dealt with and the objectives (including the various investment objectives) of the fund. The key facts statement should be a one- or two-page simple document that is made available to prospective members when they are considering entering into a contract with the fund, and which will also allow prospective members to compare different offers more easily.

<table>
<thead>
<tr>
<th>Good Practice B.4</th>
<th>Special Disclosures</th>
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<tbody>
<tr>
<td>a. Pension entities should disclose information about the products they offer including investment options, risks and benefits, fees and charges, restrictions on transfers, fraud protection over accounts, and fees on the closure of an account.</td>
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<tr>
<td>b. Clients should also be provided with meaningful, written information on essential terms of the agreement with the pension entity.</td>
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<tr>
<td>c. The consumer should be notified of planned fee changes within a reasonable period of time prior to the date of change.</td>
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<tr>
<td>d. Pension entities should inform the consumer up-front with the nature of any guarantee arrangements covering the pension products.</td>
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<tr>
<td>e. Customers should be informed up-front on the time, manner and process of disputing information on statements and transactions.</td>
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<th>Description</th>
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<tr>
<td>In relation to Pillar II funds, there are no provisions that require disclosures to be in a form that is readable to the average consumer. The Law provides that the contributors do not pay fees directly, but the SSIA pays the fees directly to the fund managers and the fees are capped at a maximum of 2 percent of funds under management.</td>
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There do not appear to be any provisions relating to how the SSIA communicates any information with the contributors.

There are no requirements in the Law to inform consumers of changes in the fees charged to the SSIA by the fund management companies. The funds are unitized and it is understood that the consumer is only provided with the value of his or her units in the scheme.

As noted above the fund management companies cannot guarantee a profit or a specific level of yield.

Section 15 contains provisions for the resolution of disputes in court, however its scope is very narrow and does not confer any specific rights on consumers with regard to the relationship between the consumer and the SSIA.

Regarding Pillar III, there are no legal requirements for the management companies to disclose the investment risk profile of the fund or the fees attached to it. However Article 24(3) of the Law on Private Pension Funds gives the consumer the right to demand this information. This article states that upon request of a member, a pension fund shall provide him or her with detailed information that includes the following:

(i) the target level of the supplementary retirement benefit, if it has been established;
(ii) the level of the supplementary retirement benefit in case of cessation of employment;
(iii) where members bear investment risk, information on investment options, if any, and on the actual investment portfolio, and information on risk exposure and any investment-related costs;
(iv) arrangements whereby a member, in the event of cessation of employment, may transfer accrued contributions for the supplementary retirement benefit to another pension fund or pension scheme.

There do not appear to be any requirements to notify consumers of fee changes.
Funds operating in Pillar Three are entitled to offer guarantees but there are no specific obligations to disclose this fact, even within the prospectus.

There are no provisions within this Law relating to handling complaints or resolving disputes.

**Recommendation**

The Law on State Funded Pensions should be reviewed to require the SSIA to disclose specific information to consumers. Minimum information needs to cover the objectives of the scheme, the way in which the scheme operates (especially in relation to the ability of the consumer to make investment choices), the transfer requirements and the complaints handling procedures. Where the fees charged by fund management companies increase and this is passed through to the consumer via a change in units prices, the Law should require that the consumer is notified of the change. The Law should be reviewed to provide for mechanisms to resolve complaints and disputes between the consumer and the SSIA.

The Law on Private Pension Funds should be reviewed to require specific disclosure of any guarantees, details of investment risk, the right of the management company to alter fees and complaint handling procedures. The Law should require Pillar Three pension funds to notify contributors of any fee changes. The Law should also be reviewed to formalize dispute and complaint resolution procedures and should require that providers supply details of the procedures to consumers at the point of sale and when statements are issued to consumers. Although Article 24 requires pension management companies to disclose some of this information (e.g. details of investment risk), disclosure is only upon request of a pension member.

**Good Practice B.5**

**Professional Competence**

Marketing personnel and officers selling and approving transactions should have sufficient qualifications and competence, depending on the complexities of the products they sell.

**Description**

In the Pillar Two funds, there are two avenues of communication with the consumers – most consumers deal directly with the SSIA, but consumers are also entitled to deal with the fund management companies if they choose to. The Law on State Funded Pensions does not set minimum competency levels for the marketing staff of either the SSIA or the fund management companies.

Pillar Three fund operators must be licensed by the FCMC under Article 8 of the Law on Private Pension Funds. This Article appears to require the identification of an executive board and council (both terms undefined). As a prerequisite for being granted a license, these persons must give details of academic qualifications but not experience. If the constitution of these bodies is altered, there are no requirements either to notify the FCMC or that these persons be fit and proper. The very limited requirements which could be seen as some indication of professional competency do not extend past the members of the executive board and council. There are no qualification requirements specifically related to marketing persons and officers selling the products.

**Recommendation**

Both laws governing pension funds should be reviewed to ensure that any person who is dealing with consumers has reached a sufficient level of competency.

The FCMC should issue some guidance as to the minimum acceptable fit and proper requirements and the level of qualifications and competence that it expects marketing and sales persons to possess.

**Good Practice B.6**

**Know Your Customer**

Pension entities should examine important characteristics of the customer such as their age and financial position before recommending a particular pension product.

**Description**

Neither law contains “know your customer” provisions. In both pillars Two and Three,
consumers are faced with a number of different investment options ranging from very conservative investments (focusing on government and private sector debt) to aggressive investment options (with equities and in certain circumstances derivatives).

Persons giving advice should understand the person’s age, attitude to risk, intentions about retirement, other assets and commitments so as to direct the consumer to an appropriate investment strategy.

**Recommendation**
Both laws governing the pension industry should be reviewed to create an obligation on all persons whom consumers may seek and ask for advice, to obtain sufficient information to understand the person’s financial position, attitude to risk and financial objectives. This information should be recorded and available for review, and pension providers should be able to demonstrate that any advice is appropriate having regard to the information obtained from the consumer.

As part of its review process, the FCMC should ensure that the providers are making appropriate enquiries of potential customers and are offering products that are consistent with the customer’s disclosures.

**Good Practice B.7**

**Contracts**
There should be consistent contracts for pension products and the contents of a contract should be read by the customer or explained to the customer before it is signed.

**Description**
In Pillar Two all members contract with the SSIA, which is effectively the manager of the Pillar Two scheme, so that all the contracts are the same. There are no provisions in the Law that govern the contents of the contract. There are no formal obligations on the staff of the SSIA to explain the contract or ensure that the consumer has read and understood it.

In Pillar Three funds, under Article 10(3) of the Law on Private Pension Funds, the FCMC has a role in relation to membership contracts. The Law states that a pension fund shall be entitled to conclude individual membership contracts in accordance with the provisions submitted to the FCMC, where within ten business days of the receipt of the provisions of an individual membership contract the FCMC has not raised substantiated objections as to their compliance with the requirements of this Law. The FCMC expresses a view on the compliance of individual contracts with the provisions of the Law but not on the understandability of the contracts. In practice, because of the role of the FCMC, the membership contracts are relatively standardized across the industry.

Article 10(8) of the Law on Private Pension Funds requires that, at the point of sale, staff of pension fund management companies explain to potential contributors the main contract terms, especially deduction amount, conditions regarding termination of membership and retirement benefits arrangements.

**Recommendation**
The Law on State Funded Pensions should be reviewed with the object of ensuring that the contents of contracts are explained to consumers before they are concluded, or at least that the relevant staff make sure that the consumers have read and understood the contents of the contract.

**Good Practice B.8**

**Cooling-off Period**
There should be a reasonable cooling-off period associated with any voluntary pension product.

**Description**
In the Pillar Two arrangements, while contributions are mandatory, participants can transfer between funds run by the same fund manager twice a year and between fund managers annually. In other words, consumers are given limited investment choice. There are no provisions within the Law on State Funded Pensions that give the consumer a cooling-off period after he or she has exercised his or her investment choice.
Although not specifically provided in the Law on Private Pension Funds, it is understood from discussions with the industry that there is a 15-day cooling-off period for applications made over the internet. It is noted that there is total portability of funds at any stage and there are no exit fees charged. However, given that funds paid into Pillar Three funds are preserved until retirement, consumers should have a statutory cooling-off period irrespective of how the application was made.

**Recommendation**

The Law on Private Pension Funds should be reviewed to ensure that all consumers have a cooling-off period during which they can cancel a contract entered into with a Pillar Three pension fund. The Law should ensure that consumers are made aware of their rights in this regard.

The Law on State Funded Pensions should be reviewed to ensure that persons who are transferring between investment options are entitled to a cooling-off period.

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**SECTION C**

**CUSTOMER ACCOUNT HANDLING AND MAINTENANCE**

**Good Practice C.1**

| a. | There should be a timely delivery of periodic statements and alerts pertaining to each account, at a frequency and in the form agreed between the customer and pension entity. |
| b. | Customers should receive a regular streamlined statement of their account that provides comprehensive details of account activity, in an easy-to-read format, to make reconciliation easy for the customer. |
| c. | Customers should have a means to dispute the accuracy of the transactions recorded in the statement within a stipulated period of time. |
| d. | When customers sign up for paperless statements, the pension entity should ensure that the consumer is able to read and understand the online statements. |

**Description**

Section 10 of the Law on State Funded Pensions sets out the obligations of the SSIA. Specifically, subsection 2 requires the SSIA to inform periodically the participants of the funded pension scheme regarding the state of their accounts, as well as regarding other significant changes in operation of the funded pension scheme. The contents of the statements have not been regulated and there is no indication of what constitutes “periodically”. The practice until quite recently was to send statements to consumers annually. This practice has been changed to allow the SSIA to issue statements on demand and to have them available on the internet for those consumers who have access to the service. It is understood that this was a cost savings initiative. There are no provisions within the Law that regulate the style, form or content of these statements.

Section 15 contains provisions on dispute procedures. The Section states: “Disputes arising due to contributions not made by the employer, as well as claims of the Agency against managers of funds and holders of funds regarding covering of losses shall be adjudicated in court according to the claim procedure, but in the case of the insolvency of the employer, manager of funds or custodian – in accordance with procedures prescribed by the Law on the Insolvency of Undertakings and Companies or by the Credit Institutions Law.” This does not appear to contemplate the situation where a consumer wants to dispute the information of the statements provided by the SSIA.

Article 24 of the Law on Private Pension Funds sets the obligations of private pension funds regarding account statements. In particular, “at least once a year the executive board of a pension fund shall send to each member of a pension scheme a written statement on the respective reporting period. The statement shall indicate the contributions for the account of the member of a pension scheme paid during the reporting period, accrued supplementary retirement benefit in its individual account, and an indication as to where the annual report/accounts of the pension fund is/are available to members of a pension scheme.”
There are no provisions in the Law that regulate the style of these statements. Also, the information that is required is limited. For example there is no requirement for the provider to disclose the amount of fees that has been deducted from the account of the participant.

There are no provisions for consumers to opt out of receiving paper based statements.

There do not appear to be any provisions in the Law which cover the rights of the consumers to dispute the accuracy of the account statement sent by the pension fund.

**Recommendation**

The SSIA should reestablish its practice of sending automatic annual statements of account to contributors unless they have elected to receive a paperless statement.

The Law on State Funded Pensions should be reviewed to specify the periodicity of statements, the contents and the style of those statements. The Law should contain the right of consumers to elect to receive this information electronically and specify the contents and style of statements received electronically.

The Law on Private Pension Funds should be reviewed to include a mechanism whereby contributors can dispute the accuracy of those statements. The Law should clarify whether the providers have the alternative of issuing paperless statements and, if so, the Law should specify conditions concerning the issue of statements in this form.

### SECTION D PRIVACY AND DATA PROTECTION

**Good Practice D.1 Confidentiality and Security of Customers’ Information**

Customers of pension entities have a right to expect that their financial activities will be private from federal government scrutiny and anyone else. The law should require pension entities to ensure that they protect the confidentiality and security of a customer’s information against any anticipated threats or hazards to the security or integrity of such information; and against unauthorized access to or use of customer information that could result in substantial harm or inconvenience to any customer.

**Description**

There are no specific requirements within any of the pension legislation relating to the protection of information that is held by either the SSIA or the Pillar Three pension funds. However, these parties are required to observe the Personal Data Protection Law.

**Recommendation**

Consideration should be given to incorporate the relevant sections of the Personal Data Protection Law in both pension Laws. Otherwise, the FCMC needs to ensure that SSIA and Pillar Three companies are aware of and comply with any changes in the Personal Data Protection Law.

**Good Practice D.2 Sharing Customer’s Information**

- Pension entities should inform the consumer of third-party dealings that require sharing customers’ information.
- Pension entities should explain how they use and share customers personal information Pension entities should be obliged not to sell or share account or personal information to outside companies that use the information only for telemarketing or direct mail marketing.
- The law should allow a customer to stop or "opt out" of certain information sharing and the pension entities should inform the customers of their options.
- The law should prohibit the disclosure of customers’ information by third parties.

**Description**

Again, there are no provisions within either of the Latvian pension laws that govern how
providers can deal with the information that they hold with respect of their consumers.

The Pillar Two fund managers do not possess information concerning the identity of the persons whose money they manage because of the "blind" structure of the second pillar. All the personal information of participants in this pillar including contact details reside with the SSIA.

The Pillar Three pension fund managers are generally parts of financial groups that include insurance companies or banks. These parties may have an incentive to share data to cross sell financial information.

The pension regimes rely on the Personal Data Protection Law. Article 8 of the Law provides that, at the request of the data subject, the data processors should provide information on third-party dealings and on how they use and share the customers’ personal information. Article 19 allows the pension member to not give consent to sharing data for commercial purposes.

Recommendation

There should be explicit requirements in these laws that govern what the SSIA and Pillar Three companies must inform their contributors about the uses to which their data will be put. The contributors should be given the right to opt out.

Consideration should be given to incorporate the relevant provisions of the Personal Data Protection Law in both pension laws. Otherwise, the FCMC needs to ensure that SSIA and Pillar Three companies are aware of and comply with any changes in the Personal Data Protection Law.

Good Practice D.3

Permitted Disclosures

a. The law should state specific procedures and exceptions concerning the release of customer financial records to government authorities.

b. The law should provide for penalties for breach of secrecy laws.

Description

Neither of the pension laws contains any specific security provisions or any penalty provisions.

The Personal Data Protection Law (Articles 11 and 13) provides for permitted disclosures for law enforcement, regulatory purposes, medical emergencies, legal proceedings and similar purposes. However, the Law does not include specific administrative sanctions against a data processor for violations of its provisions.

Recommendation

There should be penalties for breaches of the confidentiality requirements that are set at a level sufficient to be a real deterrent.

SECTON E

DISPUTE RESOLUTION MECHANISMS

Good Practice E.1

Internal Dispute Settlement

a. An internal avenue for claim and dispute resolution practices within the pension entity should be required by the supervisory agency.

b. Pension entities should provide designated employees available to consumers for inquiries and complaints.

c. Pension entities should inform their customers of the internal procedures on dispute resolution.

d. The regulator or supervisor should provide oversight on whether pension entities comply with their internal procedures on consumer protection rules.

Description

There are no provisions within either law for the SSIA or the private pension managers to have an internal dispute resolution process or to appoint designated officials to handle complaints or disputes. The Law on State Funded Pensions does contain some provisions
but these provisions are limited to disputes between the SSIA and the employers of the contributors in relation to remitting contributions and between the SSIA and the fund managers whose services it uses.

<table>
<thead>
<tr>
<th>Recommendation</th>
<th>Both laws should be reviewed with a view to requiring the SSIA and the private pension fund managers to have internal dispute settlement procedures. This should involve the appointment of designated persons who are empowered to hear and make recommendations as to the resolution of complaints or disputes. The Law should require that the SSIA and the pension funds inform consumers in the prospectuses, contracts and key facts statements of the details of the internal dispute mechanism and the contact details of the relevant persons. FCMC should ensure as part of its routine on-site reviews that these parties are complying with what they have told the contributors.</th>
</tr>
</thead>
</table>

| Good Practice E.2 | **Formal Dispute Settlement Mechanisms**  
A system should be in place that allows consumers to seek third-party recourse in the event that they cannot resolve an issue with the pension entity. |
| --- | --- |

| Description | As noted above, Section 15 of the Law on State Funded Pensions contains some dispute resolution provisions. The relevant Section states:  
“Disputes arising due to contributions not made by the employer, as well as claims of the Agency against managers of funds and holders of funds regarding covering of losses shall be adjudicated in court according to the claim procedure, but in the case of the insolvency of the employer, manager of funds or custodian – in accordance with procedures prescribed by the Law on the Insolvency of Undertakings and Companies or by the Credit Institutions Law.”  

It is noted that the scope of this provision is very narrow. There are no mechanisms for the contributor to settle disputes with the SSIA if, for example, the SSIA advises the contributor incorrectly or makes errors in his or her account or does not execute his or her instructions concerning switching between funds.  

There are no mechanisms specified in the Law on Private Pension Funds that relate to how disputes with contributors are resolved. |
| --- | --- |

| Recommendation | The Law on State Funded Pensions should be reviewed to include within Section 15 the requirements to enable contributors to seek third-party recourse to resolve disputes and complaints against SSIA or fund managers -where contributors have dealt directly with the fund managers.  

The Law on Private Pension Funds should be reviewed to incorporate the manner in which contributors can seek third-party recourse to resolve complaints and disputes against pension fund management companies. |
| --- | --- |

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<tr>
<th>SECTION F</th>
<th>GUARANTEE SCHEMES AND SAFETY PROVISIONS</th>
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</table>

| Good Practice F.1 | Guarantee and compensation schemes are less common in the pensions sector than in banking and insurance. There are more likely to be broader fiduciary duties and custodian arrangements to ensure the safety of assets.  
a. There should be a basic requirement in the law that pension entities should seek to safeguard pension fund assets.  
b. There should be adequate depository or custodian arrangements in place to ensure that assets are safeguarded. |
| --- | --- |

| Description | There are no guarantee or compensation schemes within either Law.  

The assets of both Pillar Two and Pillar III funds are required to be held by a custodian according to their respective legislation. |
| --- | --- |

<p>| Recommendation | No recommendation. |</p>
<table>
<thead>
<tr>
<th>SECTION G</th>
<th>CONSUMER EMPOWERMENT</th>
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<tbody>
<tr>
<td><strong>Good Practice G.1</strong></td>
<td><em>Financial Education through the Media</em></td>
</tr>
<tr>
<td></td>
<td>a. Press and broadcast media should be encouraged to actively cover issues related to retail financial products.</td>
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<tr>
<td></td>
<td>b. Regulators and/or industry associations should provide sufficient information to the press and broadcast media to facilitate the analysis of issues related to financial products and services.</td>
</tr>
<tr>
<td><strong>Description</strong></td>
<td>It does not appear to be within the mandate of the FCMC or the CRPC to liaise with the press and broadcast media to cover issues related specifically to the pension sector.</td>
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<td></td>
<td>The Association of Private Pension Funds has as one of its longer term strategic objectives to promote interest in voluntary pensions. However there have been no initiatives undertaken to date.</td>
</tr>
<tr>
<td><strong>Recommendation</strong></td>
<td>The FCMC and the CRPC should encourage the media to cover issues relating to the industry.</td>
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<td></td>
<td>The Association of Private Pension Funds should be encouraged by the Government to promote the interests of voluntary pensions.</td>
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<tr>
<td><strong>Good Practice G.2</strong></td>
<td><em>Information Resources for Consumers</em></td>
</tr>
<tr>
<td></td>
<td>a. The government and regulators should devise, publish and distribute information resources for consumers that seek to improve consumer awareness and knowledge.</td>
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<td></td>
<td>b. Public education on consumer awareness in the area of pensions by non governmental organizations should be encouraged.</td>
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<td></td>
<td>c. The government should develop a strategy for including financial education as part of the general education curriculum.</td>
</tr>
<tr>
<td><strong>Description</strong></td>
<td>There was no evidence of activity in relation to the FCMC distributing information of a general nature to consumers to improve awareness and knowledge of the need to provide adequately for retirement.</td>
</tr>
<tr>
<td></td>
<td>The CRPC did not seem to be active in this area either. There was no evidence that financial education targeted at retirement income formed part of the general education curriculum.</td>
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