



*Unofficial translation by the Financial and Capital Market Commission*

Effective as from 24.12.2009

Published in the official newspaper "*Latvijas Vēstnesis*" No. 202 (4188) 23.12.2009

As amended by Decision No. 335 (Min. No. 49 (19)) of the Board of the Financial and Capital Market Commission of 20.12.2010.

(Published in the official newspaper "*Latvijas Vēstnesis*" No. 203 (4395) 23.12.2010, effective as of 24.12.2010)

Riga, 21 December 2009

Regulations No. 171  
(Min. No. 49 (5))

## Regulations on Core Principles of Remuneration Policies

Issued in accordance with Article 7 (1), subparagraph 1 and Article 17 (2) of the Law on the Financial and Capital Market Commission

### 1. General provisions

1. Regulations on Core Principles of Remuneration Policies (hereinafter – the Regulations) prescribe core principles of remuneration policies and are binding to the banks registered in the Republic of Latvia, as well as investment firms to which capital adequacy regulatory requirements are applicable in accordance with Article 121 of the Law on the Financial Instruments Market, considering provisions of Article 119<sup>1</sup> of this Law and which provide investment services referred to in paragraphs 5 and 6 of Article 3 (4) of the Law on the Financial Instruments Market, also insurance and reinsurance undertakings (hereinafter – the institution), pursuant to provisions of Paragraph 4 of the Regulations. Provisions of the Regulations are recommended to apply also by other investment firms, as well as investment management companies and private pension funds.

2. The institution shall comply with the provisions of the Regulations at the individual level and consolidated group or consolidated sub-group level taking account of its organisational framework, scale, nature, complexity and specifics of its activities.

3. The following terms are used in the Regulations:

3.1. internal control functions – risk control, compliance control and internal audit functions performed in the institution;

3.2. variable component of remuneration – part of remuneration depending on the performance, the framework of which can be comprised of various elements, for instance, cash payments (for instance, bonus) or non-cash payments (for instance, in the form of shares or share-linked instruments). Variable component of remuneration shall include pension benefits determined by the institution on a discretionary basis (namely – discretionary pension benefits), where its volume depends on the performance results, excluding such contributions to private pension funds of pension plans or such retiring-related expenses that are provided on an institution-wide level according to respective pension policy;

3.3. remuneration – total amount of fixed component of remuneration (usually – salary) and variable component of remuneration (where envisaged);

3.4. material variable component of remuneration – 35 percent to 60 percent (excluding) of employee remuneration in an accounting year;

3.5. particularly high variable component of remuneration – 60 and more percent of employee remuneration in an accounting year.

*(As amended by Regulations No. 335 of the Board of the Financial and Capital Market Commission of 20.12.2010 and effective as of 24.12.2010)*

4. The institution shall ensure that:

4.1. requirements of the Regulations shall be applied to all levels of the positions of the institution's organisational framework whose professional activities substantially affect the institution's risk profile, for instance, such positions as members of the executive board, employees mandated on behalf of the institution to take risks that substantially affect the institution's risk profile, to the employees performing internal control functions in the institution, as well as to the employees whose remuneration is equal or exceeds the scale of lower remuneration for the job family to the members of the executive board or employees mandated on behalf of the institution to take risks that substantially affect the institution's risk profile (hereinafter also – positions affecting the institution's risk profile);

4.2. employees subject to the requirements of the Regulations are committed to avoid applying personal hedging strategies or such remuneration or liability related insurance that could mitigate the risk of the impact of potential adjustments, determined in the remuneration policy, on the remuneration;

4.3. by paying variable component of remuneration, no instruments or techniques are used to facilitate evading compliance with the Regulations.

*(As amended by Regulations No. 335 of the Board of the Financial and Capital Market Commission of 20.12.2010 and effective as of 24.12.2010)*

5. Regulations are not binding on the fees and commissions, which the institution shall pay to intermediaries and to outsourcing service providers in case of outsourcing.

## **2. Remuneration policy**

### **2.1. Governance**

6. The institution shall ensure the development, implementation and constant maintenance of such remuneration policy for the positions affecting the institution's risk profile (hereinafter – remuneration policy) that:

6.1. does not encourage risk taking that exceeds risk tolerance determined by the institution's risk strategy;

6.2. does not limit the institution's ability to strengthen its own funds;

6.3. is in line with the institution's objectives, values, for instance, ethical standards, long-term interests laid down in the development strategy, as well as meet and facilitate sound and efficient risk management;

6.4. does not contradict with the principles for protection of client and investor interests and interests of other parties concerned;

6.5. does not allow determining the guaranteed amount of variable component of remuneration, except in cases of hiring a new employee in the first year of employment.

*(As amended by Regulations No. 335 of the Board of the Financial and Capital Market Commission of 20.12.2010 and effective as of 24.12.2010)*

7. The supervisory board of institution shall be responsible for:

7.1. determining the core principles of remuneration policy and approval of remuneration policy;

7.2. oversight of the development and implementation of remuneration policy;

7.3. determining remuneration for the members of the institution's executive board, highest level employees performing internal audit functions, as well as for employees whose remuneration is equal or exceeds the scale of lower remuneration for the job family of the members of the executive board. If the institution receives support for business activities, its supervisory board shall without delay revise remuneration for members of its executive board and other positions affecting the institution's risk profile in compliance with sound and efficient risk management and long-term growth, as well as perform its further revising in line with changes in the institution's financial standing;

7.4. direct monitoring of remuneration for the highest level employees performing risk control and compliance control functions;

7.5. revising the core principles of remuneration policy on a regular basis but not less than once a year to ensure compliance with current activities of the institution and its development strategy, as well as changes in external factors;

7.6. determining the procedure for auditing the implementation of the institution's remuneration policy in compliance with the approved remuneration policy (for instance, the institution's supervisory board determines that compliance shall be audited and evaluated by internal control functions regularly but not less than once a year);

7.7. determining the reporting procedure to the supervisory board of institution regarding audits performed by internal control functions and conclusions drawn, as well as an impact of remuneration policy on the institution's risk profile and the quality of risk management.

*(As amended by Regulations No. 335 of the Board of the Financial and Capital Market Commission of 20.12.2010 and effective as of 24.12.2010)*

8. The institution's executive board shall be responsible for the development of remuneration policy in compliance with the core principles of remuneration policy determined by the institution's supervisory board as well as to ensure the development and approval of relevant internal procedures and implementation, considering that:

8.1. remuneration for internal control functions is determined in accordance with objectives set for internal control functions and irrespective of the performance in the business areas controlled by internal control functions;

8.2. remuneration for the function of actuary and remuneration for a responsible actuary are commensurate with the role (significance) of the performer of above function of actuary and actuary in the respective insurance undertaking or reinsurance undertaking.

The institution's executive board shall ensure that performers of positions affecting the institution's risk profile are informed regarding indicators and methods used in the evaluation of their performance and determining the variable component of their remuneration, as well as ensure that internal regulations for determining the remuneration, including an assessment process and its outcome, are sound, documented and internally transparent as far as required for performance of functions or duties or as far as related to the relevant employee.

*(As amended by Regulations No. 335 of the Board of the Financial and Capital Market Commission of 20.12.2010 and effective as of 24.12.2010)*

9. The institution, in line with its scale, nature, complexity and specifics of its activities, as well as its organisational framework, shall evaluate the necessity of

establishment of remuneration committee. The remuneration committee shall be responsible for preparing internal regulations approved by the institution's supervisory board and related to the remuneration, including preparation of the internal procedures that have an impact on the institution's risk profile and risk management quality.

The remuneration committee shall prepare internal regulations taking into account long-term interests of the institution's shareholders, investors and other stakeholders concerned.

In accordance with authorization of the institution's supervisory board the remuneration committee may be responsible also for determining remuneration for the members of executive board, highest level employees performing internal audit functions, as well as for employees whose remuneration is equal or exceeds the scale of lower remuneration for the job family of members of the executive board, as well as direct monitoring of remuneration for the highest level employees that perform risk control and compliance control functions.

A member of the institution's supervisory board shall be appointed as chairperson of the remuneration committee. Only members of the institution's supervisory board may be appointed as members of the remuneration committee.

The institution shall ensure that the evaluation and decisions made regarding the necessity of establishment of the remuneration committee are documented.

*(As amended by Regulations No. 335 of the Board of the Financial and Capital Market Commission of 20.12.2010 and effective as of 24.12.2010)*

10. Employees who perform internal control functions and employees who perform personnel management function in the institution as well as shareholders and external experts, where appropriate, shall be also engaged in the development and implementation of remuneration policy and relevant internal procedures and ensuring compliance thereof. Above employees, members of remuneration committee, shareholders, external experts, as well as members of board of directors responsible for the institution's remuneration policy shall:

- 10.1. have relevant expertise;
- 10.2. be functionally independent from the business units they control;
- 10.3. have the necessary mandate to perform their functions and obtain information;
- 10.4. be capable of providing an independent and competent assessment on the remuneration policy and compliance thereof, as well as its appropriateness to the activities of the institution, including its impact on the institution's risk profile and the quality of risk management, capital maintenance and liquidity management.

## **2.2. Core principles of remuneration policy**

11. Core principles of remuneration policy shall determine:

11.1. objectives of remuneration policy, for instance, recruitment and motivation of qualified employees;

11.2. elements of remuneration, including salary, bonus, incentive schemes aimed at long-term results, shares or share-linked instruments, severance pay due in case of termination of labour or authorization contract, contributions to the private pension funds of pension plans, discretionary pension benefits and other retiring-related expenses in accordance with the institution's pension policy, which shall be in line with the institution's objectives, values and long-term interests laid down in the institution's development strategy and other;

11.3. financial and non-financial indicators and methods used in evaluation of the performance and determining the variable component of remuneration for the positions

affecting the institution's risk profile. The institution shall ensure documenting of the assessment and adopted decisions on determining the positions affecting the institution's risk profile;

11.4. measures for preventing conflict of interest, for instance, eliminating a possibility for the members of the institution's executive board to determine or participate in determining their own remuneration;

11.5. commensurate proportion between the fixed and variable components of remuneration for positions affecting the institution's risk profile, including the structure of variable component of remuneration and the upper margin of variable component of remuneration, taking into account the business areas where the respective employee carries out professional activities, conditions and specifics of activities. The institution shall ensure sufficient proportion of fixed component of remuneration to allow the institution to apply a flexible remuneration policy regarding the variable component of remuneration, including the possibility to withhold the variable component of remuneration, for instance, in case of deterioration of financial standing and solvency of the institution, taking into account considerations regarding ensuring capital adequacy in the long-term;

11.6. procedure for deferment of material and a particularly high variable component of remuneration, taking into account that in case of determining the material variable component of remuneration not less than 40 percent (in case when a particularly high variable component of remuneration is determined – not less than 60 percent) of variable component shall be deferred for a period not less than three to five years depending on the level of position or responsibility and during which underlying performance, sustainability and relevant risks can be evaluated. Deferral period for the variable component of remuneration shall be set in accordance with the business cycle, nature of business, its risks and activities of employee concerned;

11.7. procedure for determining a particularly high variable component of remuneration, taking into account that in case of a particularly high variable component of remuneration not less than 50 percent of it shall be defined in the form of non-cash instruments, in case the institution's equity securities are admitted to trading on a regulated market. The institution shall determine appropriate retention policy for above mentioned non-cash instruments, i.e. the number of years where the recipient of relevant non-cash instruments is not eligible to sell the instruments, in order to ensure compliance of incentive schemes with long-term interests of institution, as set in the remuneration policy;

11.8. terms of payments of reducing or withholding severance pays, which exceed amounts of severance pay determined in the Labour Law, in case of early termination of labour contract or authorization contract, if any drawbacks or mistakes are made during operation of relevant performers of positions affecting the institution's risk profile. The institution shall take into account that in case of termination of labour contract or authorization contract payments shall reflect performance achieved over the duration of legal relationships of labour;

11.9. payment conditions for the variable component of remuneration for those positions affecting the institution's risk profile irrespectively of its structure (the institution's shares, share-linked instruments, cash or any other means of payment) and acquisition of vested rights to it, taking into account that:

11.9.1. actual payment of variable component of remuneration, including deferred part, shall be carried out or in line with provisions of Paragraph 11.9.2 hereof vested rights to it shall be acquired according to the business cycle and business risks of the institution, as well as in case the payment conforms to the institution's financial standing and performance of the institution, relevant performers of positions affecting the institution's risk profile and relevant structural unit. The institution shall reduce the payment of variable component of

total remuneration including also the payment of total deferred portion of variable component of remuneration, in case of subdued or negative financial performance occurs. The institution shall ensure application of such mechanisms as requiring repayment of paid-out variable component of remuneration or reduction in the total deferred portion of variable component of remuneration partially or in full, if it has been assigned for the performance based on data which, as later detected, have been maliciously misinterpreted (clawback), or reduction in the deferred portion of variable component of remuneration to which vested rights have not been acquired, based on actual performance results (malus);

11.9.2. vested rights to the payment of deferred portion of variable component of remuneration shall be acquired proportionally to the deferral period (number of years) but not before 12 months upon determining the variable component of remuneration. Prior to acquiring vested rights to the deferred portion of variable component of remuneration it is adjusted (reduced) if required, considering risks that are not included in the initial calculation, which emerged during the period of deferral of variable component of remuneration, and that are associated with performance according to which the variable component of remuneration was determined. The institution shall take into consideration that actual pay-out of deferred portion of variable component of remuneration may be carried out after acquiring vested rights to it;

11.9.3. carrying out actual payments of particularly high variable component of remuneration, including deferred portions, provisions of Paragraph 11.7 of Regulations hereof shall be applied both to the deferred and non-deferred part of variable component of remuneration;

11.10. payment conditions related to pension benefits which are part of variable component of remuneration (namely – discretionary pension benefits), in case the institution's equity securities are admitted to trading on a regulated market in line with following requirements:

11.10.1. if the labour relations are terminated before reaching retirement age, the institution shall ensure that discretionary pension benefits in the form of non-cash instruments are held by the institution for a period not less than five years, i.e. discretionary pension benefits shall be paid in the form of non-cash instruments five years after termination of labour contract in case of early retirement;

11.10.2. upon reaching retirement age the institution shall ensure that discretionary pension benefits are paid to the employee in the form of non-cash instruments and the institution's retention policy defined for non-cash instruments has been applied to discretionary pension benefits, taking into account that a retention period for above instruments cannot be less than five years, i.e. the employee may sell discretionary pension benefits paid in the form of non-cash instruments no earlier than five years after reaching of retirement age.

*(As amended by Regulations No. 335 of the Board of the Financial and Capital Market Commission of 20.12.2010 and effective as of 24.12.2010)*

### **2.3. Performance assessment and determining of variable component of remuneration**

12. In the assessment of performance not only such financial indicators as, for instance, income or turnover shall be used. If the financial indicators calculated on the basis of accounting data are used for the performance assessment purposes (for instance, accounting profit), the institution shall take into account that such indicators cover performance over previous periods, but do not cover risks that may expose the institution to loss in the future. The institution shall develop methods for adjusting the financial indicators used for the

calculation of the amount of variable component of remuneration for individual bonus or for bonus pools in accordance with the organizational structure of the institution – at the level of structural unit, institution, consolidated group or consolidated sub-group – taking into account:

12.1. evaluation of current risks and likely risks associated with performance;

12.2. cost of capital and expenses required to ensure liquidity.

*(As amended by Regulations No. 335 of the Board of the Financial and Capital Market Commission of 20.12.2010 and effective as of 24.12.2010)*

13. Non-financial indicators (for instance, compliance with internal procedures and standards regulating the relationships with clients and investors or compliance with set limits) shall be used in the assessment of performance, and they shall be taken into account evaluating individual performance of performers of positions affecting the institution's risk profile. Assessing significance of non-financial indicators, the institution shall take into consideration that the usage of non-financial indicators is material in assessing individual performance, as a failure to comply with non-financial indicators (or partial compliance) may affect the institution's risk profile or financial results.

14. Variable component of remuneration shall be calculated in compliance with following requirements:

14.1. in determining the variable component of remuneration, combination of assessment of individual performance of relevant performers of positions affecting the institution's risk profile and performance at the level of relevant structural unit and the overall results at the level of institution, consolidated group or consolidated sub-group are taken into account, as well as assessments regarding sustainability (consistency) of performance presented by experts, for instance, risk control functions;

14.2. in assessing performance, multi-year performance results are taken into account to ensure that the assessment process is based on the long-term performance.

*(As amended by Regulations No. 335 of the Board of the Financial and Capital Market Commission of 20.12.2010 and effective as of 24.12.2010)*

15. In developing methods for adjusting the financial indicators for the calculation of variable component of remuneration for positions affecting the institution's risk profile it is recommendable to indicate:

15.1. risks related or probably associated with the scope of activities of positions affecting the institution's risk profile;

15.2. internal control elements for reducing current risks and likely risks;

15.3. the period that is required to assess results of activities performed by the positions affecting the institution's risk profile.

### **3. Disclosure of information on remuneration policy**

16. *(Deleted in accordance with Regulations No. 312 of the Board of the Financial and Capital Market Commission of 13.11.2010 and effective as of 31.12.2010)*

16.<sup>1</sup> The institution shall disclose information on its remuneration policy and practice in accordance with provisions of Paragraph 28 of the Regulations No. 61 of the Financial and Capital Market Commission (Regulations on Information Disclosure and Institution's Transparency of 02.05.2007).

*(As amended by Regulations No. 335 of the Board of the Financial and Capital Market Commission of 20.12.2010 and effective as of 24.12.2010)*

17. *(Deleted in accordance with Regulations No. 312 of the Board of the Financial and Capital Market Commission of 13.11.2010 and effective as of 31.12.2010)*

17.<sup>1</sup> The institution not later than until 1 April of subsequent year shall submit to the Financial and Capital Market Commission information on those employees of the institution whose remuneration in the accounting year is equal or exceeds EUR 1 million equivalent in lats at the exchange rate as set by the Bank of Latvia specifically indicating the position and type of activity of the employee, as well as the distribution of remuneration into various elements.

*(As amended by Regulations No. 335 of the Board of the Financial and Capital Market Commission of 20.12.2010 and effective as of 24.12.2010)*

#### **4. Closing provisions**

18. The institution, which has been registered before the Regulations take effect, shall implement provisions of the Regulations not later than by 31 December 2010. Information referred to in Paragraphs 17.6.1, 17.6.2 and 17.6.5 of the Regulations for the first time shall be disclosed by the institution for the year 2009.

19. The institution shall apply amendments to Paragraphs 3, 4, 6, 7, 8, 9, 11, 12 and 14 of Regulations hereof regarding variable component of the remuneration which is determined based on the performance results for the year 2010 but not yet paid out or to which vested rights are not yet acquired.

*(As amended by Regulations No. 335 of the Board of the Financial and Capital Market Commission of 20.12.2010 and effective as of 24.12.2010)*

20. The amendment regarding supplementing Paragraph 16.<sup>1</sup> of Regulations hereof shall take effect simultaneously with the Financial and Capital Market Commission's Regulations No. 312 (Amendments to Regulations on Information Disclosure of 13.11.2010) taking effect.

*(As amended by Regulations No. 335 of the Board of the Financial and Capital Market Commission of 20.12.2010 and effective as of 24.12.2010)*

#### **Reference to the European Union Directive**

The Regulations contain provisions arising from Directive 2010/76/EU of the European Parliament and of the Council of 24 November 2010 amending Directives 2006/48/EC and 2006/49/EC as regards capital requirements for the trading book and for re-securitisations, and the supervisory review of remuneration policies.

*(As amended by Regulations No. 335 of the Board of the Financial and Capital Market Commission of 20.12.2010 and effective as of 24.12.2010)*

Chairwoman  
Financial and Capital Market Commission

I. Krūmane