

Decision No. 149  
(min. No. 44 paragraph 5 )  
of the Board of the Financial and Capital Market Commission

Riga, 13 November 2009

ON AMENDING AND PROLONGING DECISION NO. 1 (MIN. NO. 85, §3) ADOPTED  
BY THE CABINET OF MINISTERS AND FINANCIAL AND CAPITAL MARKET  
COMMISSION OF 01.12.2008 ON THE SETTING OF RESTRICTIONS ON THE  
FULFILMENT OF OBLIGATIONS BY THE JSC "PAREX BANKA"

1. On 1 December 2008, the Cabinet of Ministers of the Republic of Latvia and the Financial and Capital Market Commission (address: Kungu iela 1, Rīga, LV-1050, LATVIA) (hereinafter also – the Commission) adopted a decision No 1 (min. No. 85, §3) on the setting of restrictions on the fulfilment of obligations by the JSC "Parex banka" (hereinafter – the Decision).

2. The following restrictions were set on the fulfilment of obligations by the JSC "Parex banka" (registration No.: 40003074590, registered address at Republikas laukums 2a, Riga, LV-1522, Latvia) (hereinafter – the Bank) with the above Decision:

2.1. to impose a ban on the Bank to carry out debit transactions in any currency, including through online banking, ATMs and by cash, with clients - natural persons for the amount that exceeds LVL 35 000 per calendar month;

2.2. to impose a ban on the Bank to carry out debit transactions in any currency which are not intended for the purposes of economic activity, including through online banking, ATMs and by cash, with clients - legal persons;

2.3. to impose a ban on the Bank to carry out debit transactions in any currency which are intended for the purposes of economic activity, including through online banking, ATMs and by cash, with clients - legal persons:

2.3.1. with staff fewer than 10 employees as of 31 December 2007 and that exceeds the amount of 35 000 lats per calendar month;

2.3.2. with staff between 11 and 250 employees as of 31 December 2007 and that exceeds the amount of 350 000 lats per calendar month;

2.4. to impose a ban on the Bank to issue new loans and increase loan limits on the existing loans as well as a ban to perform any transactions in the financial instruments, except *repo* deals;

2.5. to impose a ban on the Bank without permission from the authorized representative:

2.5.1. to conduct any transactions (placement of funds in the interbank market, conversion of non-cash foreign currency, disposal of any assets, encumbrance of assets etc.), which are performed in the name of the Bank and relevant payments;

2.5.2. to dispose or encumber the Bank's property, its investments in the financial instruments and in the capital of other commercial companies, to suspend operation of its branches or structural units;

- 2.5.3. to waive any right to demand;
- 2.5.4. to issue warranties, guarantees and provide documentary loan service, as well as modify, renew or terminate existing transactions;
- 2.5.5. to issue any type of powers, incl. power of attorney, to any person to undertake obligation in the name of the Bank, as well as to extend the validity of existing powers;
- 2.5.6. to waive the right to possession or holding or the right to use any property or belonging that has come into the possession of the Bank under its legal rights, except the storage of client valuables in the Bank;
- 2.5.7. to acquire any fixed assets or intangible assets;
- 2.5.8. to modify the Bank's general action rules, price list and transaction commission;
- 2.6. to determine that restrictions on the settlement of liabilities are not applicable to:
  - 2.6.1. payments into the national budget;
  - 2.6.2. payments to the state and local government authorities (incl. the Bank of Latvia, the Commission, the Deposit Guarantee Fund);
  - 2.6.3. transactions with the Bank of Latvia;
  - 2.6.4. acquisition of the Republic of Latvia treasury bills;
  - 2.6.5. payments to the commercial companies which spheres of activity encompass commodity production and provision of services to the sectors governed by the state and local government authorities;
  - 2.6.6. deposit interest payments;
  - 2.6.7. client payments to the Bank and its subsidiaries.

3. With the 19.06.2009 Decision No. 81 (min. No. 24, paragraph 11) of the Board of the Commission, the period of restrictions on the settlement of liabilities set by the Decision No. 1 of the Cabinet of Ministers and the Financial and Capital Market Commission of 01.12.2008 (min. No. 85, §3) on the setting of restrictions on the fulfilment of obligations by the JSC "Parex banka", was extended until 30.11.2009.

4. In accordance with Section 113 (1) of the Credit Institution Law if the Commission ascertains that a credit institution fails to adhere to the provisions of this Law, directly applicable rules issued by European Union institutions, or decisions or regulations issued by the Financial and Capital Market Commission; or if the activities of a credit institution are threatening its stability or solvency, security or stability of the credit institution sector in Latvia, or if such activities impose threat to cause significant loss to the national economy, or if an excessive outflow of deposits or other assets is occurring from a bank, the Financial and Capital Market Commission by adopting the decision shall have the right to implement one or more of the following actions, incl.:

- to establish restrictions on the rights and actions of the credit institution, including entirely or partially suspending the provision of financial services, as well as restrictions on fulfilment of obligations, except for the restrictions on fulfilment of obligations referred to in Sub-paragraph 5 of Paragraph One (Sub-paragraph 4 of Section 113 (1) of the Credit Institution Law);
- to impose upon the bank restrictions on execution of deposit liabilities (Sub-paragraph 5 of Section 113 (1) of the Credit Institution Law).

Section 114 of the Credit Institution Law stipulates that a decision to impose deposit restrictions may be adopted by the Financial and Capital Market Commission only with regard to a bank, which at the time of adoption of such decision is capable of satisfying the

legal claims submitted by its creditors. The decision to impose deposit restrictions shall set forth the types of restrictions and a period of effectiveness, which shall not exceed 12 months.

In accordance with Amendments to the Credit Institution Law of 22.10.2009 the duration of above restrictions may be extended for the bank to which support for performing commercial activities is granted till the end of granting support (Section 114, Paragraph 2.<sup>1</sup> of the Credit Institution Law). Legislator has adopted such legal provision in view to ensure the maximum protection of state interests and the purpose of support for commercial activities – to assist in restructuring of the bank in difficulty and restore its liquidity.

Section 99.<sup>1</sup> (1) of the Credit Institution Law prescribes that in order to ensure the security, stability and development of Latvia's credit institution sector, the Financial and Capital Market Commission shall perform supervision of credit institutions.

In accordance with Section 99.<sup>1</sup> (2) of the Credit Institution Law, the Commission has a duty to take measures without delay in accordance with the specifications of the Law in order to prevent deficiencies in the operations of credit institutions and the credit institution sector, which threaten or may threaten the stable operation of a credit institution or the credit institution sector on the whole, interfere in the conduct of proper transactions, the provision of financial services or may cause significant loss to the overall State economy.

5. The Commission established the following actual state of affairs:

5.1. On the basis of information in the Commission's possession, financial statements submitted by the Bank and operative data, the Commission draws a conclusion that the Bank is solvent.\*

To ensure capital adequacy in the JSC "Parex banka", on 13.10.2009 the Cabinet of Ministers passed the Decision (min. No. 69, §78), according to which the State must indirectly, through the state joint stock company "*Privatizācijas aģentūra*" (Latvian Privatization Agency), increase a qualifying holding in the Bank by the acquisition of newly issued 24 250 000 name shares without voting rights at nominal value of one lats. On 29.10.2009, the Bank's share capital was increased by LVL 24 300 000.

5.2. The Commission notes that a number of essential measures have been taken in the Bank (increasing the Bank's capital, stabilizing deposit base) in order to stabilize activities of the Bank and to meet regulatory provisions of the law, and as a result though the Bank's performance has improved, however, at the moment the Bank is not yet able to fully meet all the requirements as set by law, namely,\* and the above may lead to conclusion that the Decision No 81 of 19.06.2009 regarding extension of the period of restrictions on the fulfilment of obligations had prevented from a larger decrease in the deposits.

Currently the Bank ensures compliance with liquidity requirements; however, the Bank has not still succeeded in attracting deposits or any other alternative resources and as a result, the lifting of the restrictions imposed on the Bank's activities is not possible. Prolonging of the above restrictions will ensure moderate changes.

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\* Restricted Access Information according Section 5. and Section 7. of the Freedom of Information Law

In making the Decision on extending the restrictions on the fulfilment of liabilities of the Bank, the Commission takes into account information submitted by the Bank: on 31.10.2009 the number of the Bank's clients – depositors was about 243 000 clients. Meanwhile, the restrictions on the fulfilment of liabilities set in the Decision presently are applicable to less than 1 000 clients of the Bank. \* Considering the above, the Commission draws a conclusion that the number of clients, whose legal interests would be restricted by the extension of the Decision, is rather insignificant in comparison with the number of rest depositors whose interests will be protected by ensuring sound operation of the Bank.

6. In assessing the Bank's financial standing, the Commission takes into account the measures taken by the State to improve the Bank's financial ratios and ensure its stability:

6.1. On 19.03.2009, the Bank reached an agreement on modifying the syndicated loan contract conditions, paying out EUR 232 500 000 to lenders. Next syndicated loan payments are scheduled in February 2010 (EUR 310 000 000) and in May 2011 (EUR 232 500 000). Repayment of the remaining syndicated loan has been guaranteed by the State.

6.2. On 16.04.2009, Prime Minister V. Dombrovskis, the state JSC "Privatizācijas aģentūra" Board Chairman A. Grants and the Bank's Board Chairman N. Melngailis signed an agreement with the European Bank for Reconstruction and Development (hereinafter – also EBRD) on the acquisition of the Bank's shares (25 percent plus one share). On 23.07.2009, the agreement was modified and signed with the EBRD, to provide that terms of the transaction conform to the amount of State support as authorized by the European Commission and to ensure a two-stage completion of transaction. The first stage ended on 03.09.2009 and as a result EBRD acquired 51 444 325 shares, i.e., 25% plus one share. The second stage of transaction according to which the EBRD acquires 6 062 500 more shares of the Bank, will take place after increasing of the remaining Bank's share capital. Upon closing of transaction the EBRD will have a total of 57 506 825 shares in the Bank.

After closing the transaction, EBRD is planning to additionally invest EUR 3 600 000 in the Bank's subordinated capital. Currently, the EBRD subordinated loan to the Bank constitutes EUR 18 400 000. By the end of 2009, total EBRD loan to the Bank could amount to EUR 22 000 000.

6.3. In addition to the capital injection by the state JSC "Privatizācijas aģentūra" into the raising of the Bank's capital by LVL 140 750 000 on 22.05.2009 and issuing a subordinated loan of LVL 50 270 000, on 29.10.2009 the Bank's share capital was raised by LVL 24 300 000 through the acquisition of newly issued 24 250 000 name shares without voting rights at nominal value of one lats.

7. Considering consistent improvement in the Bank's liquidity ratios already over several months, as well as the measures referred to in point 6 hereof have resulted in the improvement of the Bank's performance indicators, the Commission holds the opinion that when prolonging the period of restrictions on the settlement of liabilities as set by the Decision, according to which the outflow of large amounts of funding from the Bank will be prevented, it would be advisable to reduce the amount of restrictions on the settlement of liabilities, thus increasing the

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\* Restricted Access Information according Section 5. and Section 7. of the Freedom of Information Law

Bank's ability to provide financial services, its competitiveness and re-establishing depositors' confidence in the Bank's solvency.

7.1. Currently, several clients (institutional clients and companies subject to the supervision of the Public Utilities Commission), whose current account balances are subject to the restrictions imposed by the Decision, have shifted their incoming payments arising from the economic activities to another banks, while outgoing payments have been performed from the Bank. Therefore, monthly debit transaction limit is crucial instead of limits on payment targets. The Commission has already favoured lifting of enhanced control over compliance of economic activities' payments for the state/local government institutions and state/local government-owned undertakings.

7.2. The Commission is of the opinion that monthly limits on the client debit transactions set by the Decision could be increased by 5% (five percent) of the credit turnover of the previous month's incoming assets in the Bank under the condition that the Bank would be capable of ensuring operational risk control over the above process. Maximum increase in limits is LVL 150 000. Minimum credit turnover required for raising limits is LVL 100 000 and incoming amounts must be held in the Bank not less than 3 (three) days. Mitigation of such restrictions would facilitate a gradual decrease in the client funding to which restrictions refer, while the amount of the deposits in the Bank exempted from restrictions would grow and the Bank would continue increasing transactions performed by current and potential Bank's clients.

7.3. The Commission believes that the ban on lending referred to in point 10.6 of the Decision should not be applicable to granting new loans within framework of credit programmes of the European Investment Bank, European Investment Fund and European Bank for Reconstruction and Development; as well as micro loans for consumption granted in cooperation with American Express. The above loans the Bank could issue under the condition that the Bank has agreed with the Commission beforehand all the relevant crediting policies and procedures, as well as the credit risk limiting and controlling system.

8. Taking into consideration above, the Board of the Commission had drawn up a draft decision, which was forwarded by letter No 05.01.01.015/4287 to the Bank on 11.11.2009, notifying at the same time that the Board of the Commission would discuss the issue on amending and extending duration of the Decision in the meeting of the Commission's Board on 13.11.2009 and requesting to submit to the Commission in writing the Bank's opinion in the administrative case until 13.11.2009 or to participate in the 13.11.2009 meeting of the Board of the Commission, if the Bank's representatives wished to express their opinion regarding the administrative case attending the meeting in presence.

On 13.11.2009 the Commission received the Bank's letter No 2.-01/79 "On approving the draft amendments and wording of restrictions on the fulfillment of obligations by JSC "Parex banka"", where the Bank had provided their explanations regarding the administrative case.

At the 13.11.2009 meeting of the Board, the Commission heard oral explanations provided by the Bank's representatives Nils Melngailis un Guntis Belavskis.

When taking this Decision, the Commission examined the written and oral explanations provided by the Bank's representatives.

9. Considering the above Bank's financial ratios, the actual state of affairs and the State activities aimed at the improvement of the Bank's financial ratios and ensuring stability, conclusions might be drawn that the Bank's financial stability is not yet sufficient to lift the restrictions on the settlement of liabilities. Though there has been a steady improvement in the Bank's liquidity ratios already for several months, an increase in the resident transactions still does not counterbalance a decrease in deposits in the non-resident segment to the extent to lift the restrictions in full without any additional risk regarding liquidity insufficiency. Considering that the Bank has a significant role in the Latvia's financial system overall, the Commission is of the opinion that the prolonging of the Decision regarding restrictions on the settlement of liabilities would be desirable. Legal (legitimate) goal of the Commission in prolonging the Commission's Decision regarding the restrictions on the settlement of liabilities, pursuant to Section 113 (1), and Section 114 (1) and (2.<sup>1</sup>) of the Credit Institution Law, is to ensure protection of depositors and stability of the financial and capital markets in accordance with the Commission's goals as stipulated in Article 5 of the Law on the Financial and Capital Market Commission. Besides, the will of legislator is to be considered - to provide for maximum state interest protection in the period of time when the support for performing commercial activities is extended to the Bank, authorizing the Commission to extend the period of restrictions till the end of granting above support. Meanwhile reduction (mitigation) of restrictions on settlement of liabilities laid out in the Decision would provide for sound operation of the Bank and as large as possible benefit to the Bank's shareholders accordingly providing for meeting the State interests in recovering financial support granted to the Bank.

10. Such a decision is commensurable with the probable loss, and restrictions on the Bank's legal interests are justified by significant benefit given to the state and public, namely, legal interests of persons will be violated if the Commission does not adopt such a decision as well as if the Bank fails to meet regulatory requirements set for the purposes to maintain sound activities of credit institutions and the Commission does not take any measures to prevent threats on the Bank's activities, thus continuing exposure of the Bank to the risk that it would be incapable to duly meet its debt liabilities to the existing Bank's clients. Once the Bank's inability to meet requirements essential for their operation is identified, idleness of the Commission would lead to a conclusion that the supervisory system in Latvia is inadequately strict and professional because it allows the Latvia-registered banks to ignore regulatory requirements for ensuring the financial stability pursuant to the regulatory requirements of the European Community.

11. Notwithstanding the Bank's financial performance mentioned in point 5 of the Decision hereof, the decision to extend the restrictions on the settlement of liabilities is the most efficient measure out of all referred to in Section 113 (1) of the Credit Institution Law and extension of until the end of granting support for performing commercial activities is prescribed in Section 114 (2.<sup>1</sup>) of the Credit Institution Law. Other measures (e.g., a warning) will not be sufficiently effective to prevent an excessive outflow of funding from the Bank. Besides, the Decision is justifiable and commensurable with the measures taken by the State for improving the Bank's financial ratios and ensuring stability referred to in point 7 of the Decision hereof. Furthermore, annulment of the Bank's licence (permit) would not be commensurable with the above measures taken for ensuring the Bank's financial stability. The Decision is also legitimate due to significant benefit to the public – maintenance of the stability of financial system in contrast to short-term interests of the Bank's clients. In adopting this Decision, the Commission has taken into account the interests of any individual

who uses services of the financial system. The Commission's Decision will protect the interests of the Bank's clients and partners, in particular the interests of the settlement system participants in case of a financial shock to the Bank, which could result in serious impediments to the overall financial system and incommensurable damage to persons concerned.

12. Taking into account that the State has invested significant financial resources in the Bank and public unavailability of the Decision could have a negative impact on the public confidence in the Bank's solvency and its ability to provide qualitative financial services in the future, the Commission holds an opinion that the Decision should be made public.

On the basis of provisions of Section 99.<sup>1</sup> (1) and (2), Section 110.<sup>1</sup> (1), Sub-paragraphs 4 and 5 of Section 113 (1), Section 114 (1), (2) and (2.<sup>1</sup>) of the Credit Institution Law, Article 5 and Article 17 clause 6.<sup>1</sup> of the Law on the Financial and Capital Market Commission, Sub-paragraph 2 of Section 63 (1), Section 65 (4) and Section 66 (1) of the Administrative Procedure Law,

The Board of the Financial and Capital Market Commission d e c i d e s:

1. To express point 10 of the 01.12.2008 Decision No. 1 (min. No. 85, §3) of the Cabinet of Ministers of the Republic of Latvia and the Financial and Capital Market Commission on the setting of restrictions on the fulfilment of obligations by the JSC "Parex banka" in the following wording:

"10.1. to impose a ban on the Bank to carry out debit transactions in any currency, including through online banking, ATMs and by cash, with clients - natural persons for the amount that exceeds LVL 35 000 per calendar month;

10.2. to impose a ban on the Bank to carry out debit transactions in any currency which are not intended for the purposes of economic activity, including through online banking, ATMs and by cash, with clients - legal persons, ensuring the following control elements over the Bank's economic activities:

10.2.1. if the amount of payment does not exceed LVL 5 000 or the equivalent in foreign currency based on the currency exchange rate set by the Bank of Latvia, the client is permitted to carry out payments indicating the purpose of payment, name of commodity/service and making reference to underlying document;

10.2.2. if the amount of payment exceeds LVL 5 000 or the equivalent in foreign currency based on the currency exchange rate set by the Bank of Latvia, the Bank must examine compliance of debit operations with the client's economic activities;

10.2.3. control over the client's economic activities referred to in point 10.2 is not applicable to the state/local government institutions and state/local government-owned undertakings;

10.3. to impose a ban on the Bank to carry out debit transactions in any currency which are intended for the purposes of economic activity, including through online banking, ATMs and by cash, with clients - legal persons:

10.3.1. with staff fewer than 10 employees as of 31 December 2007 and that exceeds the amount of 35 000 lats per calendar month;

10.3.2. with staff between 11 and 250 employees as of 31 December 2007 and that exceeds the amount of 350 000 lats per calendar month;

10.3.3. with staff above 250 employees as of 31.12.2007 without any restrictions on the amount;

10.4. to determine that for those clients who do not perform any debit operations within one calendar month or do not perform debit operations in the maximum debit amount referred to in points 10.1 and 10.3, debit operation limits referred to in points 10.1 and 10.3 that are available to the client will be increased in the next calendar month by the amount of debit operation limit unutilized in the previous month;

10.5. to determine that debit operation monthly limit as set in points 10.1 and 10.3 is increased by 5% (five percent) of the credit turnover of the previous month's incoming assets in the Bank, if the minimum credit turnover is LVL 100 000 and incoming amounts are held in the Bank no less than 3 (three) days, maximum increase in the limit is LVL 150 000;

10.6. to impose a ban on the Bank to issue new loans and increase loan limits for existing loans as well as a ban to perform any transactions in the financial instruments, except *repo* deals;

10.7. the ban on the lending referred to in point 10.6 of the Decision is not applicable to granting new loans within framework of credit programmes of the European Investment Bank, European Investment Fund and European Bank for Reconstruction and Development; as well as micro loans for consumption granted in cooperation with American Express, under the condition that the Bank has agreed with the Commission beforehand all the relevant crediting policies and procedures, as well as the credit risk limiting and controlling system;

10.8. to impose a ban on the Bank without permission from the authorized representative:

10.8.1. to conduct any transactions (placement of funds in the interbank market, conversion of non-cash foreign currency, disposal of any assets, encumbrance of assets etc.), which are performed in the name of the Bank and relevant payments;

10.8.2. to dispose or encumber the Bank's property, its investments in the financial instruments and in the capital of other commercial companies, to suspend operation of its branches or structural units;

10.8.3. to waive any right to demand;

10.8.4. to issue warranties, guarantees and provide documentary loan service, as well as modify, renew or terminate existing transactions;

10.8.5. to issue any type of powers, incl. power of attorney, to any person to undertake obligation in the name of the Bank, as well as to extend the validity of existing powers;

10.8.6. to waive the right to possession or holding or the right to use any property or belonging that has come into the possession of the Bank under its legal rights, except the storage of client valuables in the Bank;

10.8.7. to acquire any fixed assets or intangible assets;

10.8.8. to modify the Bank's general action rules, price list and transaction commission;

10.9. to determine that restrictions on the settlement of liabilities are not applicable to:

10.9.1. payments into the budget of the resident country;

10.9.2. payments to the state and local government authorities of the resident country (incl. the Bank of Latvia, the Commission, the Deposit Guarantee Fund);

10.9.3. transactions with the Bank of Latvia;

10.9.4. acquisition of the Republic of Latvia treasury bills;

10.9.5. debit operations required for commercial companies, whose areas of activities are linked with production of commodities and provision of services in the sectors regulated by the state (power industry (power supply and gas supply companies), electronic communication (mail service), railway transport) and local governments (heat supply (without additional distribution of electricity), water supply and sewerage, waste disposal) regarding commodities and services of relevant sectors;

10.9.6. deposit interest payments;

10.9.7. client payments to the Bank and its subsidiaries;

10.9.8. no limits are set on the amount of transfer for the state and local government undertakings if they are the 100% state/local government-owned enterprises;  
10.9.9. legal persons, whose tariffs are regulated by the Public Utilities Commission, are permitted to perform debit operations with no limits on maximum amount;  
10.10. to impose legally binding obligation on the Bank to submit to the Financial and Capital Market Commission a report on measures taken to ensure fulfilment of the restrictions on the settlement of liabilities as determined by the decision until 27.11.2009;  
10.11. transactions in foreign currencies referred to above shall be converted into lats according to the currency exchange rate established by the Bank of Latvia at the day of transaction."

2. To extend the period of restrictions on the settlement of liabilities as set by the Decision No. 1 of Cabinet of Ministers and the Financial and Capital Market Commission of 01.12.2008 (min. No. 85, §3) on the setting of restrictions on the fulfilment of obligations by the JSC "Parex banka" until 30.06.2010.

3. To publish the Decision of the Board of the Financial and Capital Market Commission in the official gazette *Latvijas Vēstnesis*.

This Decision becomes effective on 01.12.2009.

In accordance with Section 188 (2) of the Administrative Procedure Law and Section 99.<sup>1</sup> (3) of the Credit Institution Law, appeal against the Decision of the Financial and Capital Market Commission may be lodged with the Regional Administrative Court (Jēzusbaznīcas iela 6, Rīga) within one month of notifying the addressee of this administrative act.

In accordance with Section 123 of the Credit Institution Law, appeal of the administrative act issued by the Financial and Capital Market Commission shall not suspend the execution thereof.

Deputy Chairman  
Financial and Capital Market Commission

J. Brazovskis

(signature)