

Unofficial translation

**Normative Regulations No. 29 of the Financial and Capital Market Commission**

Riga, 31 March 2020

(Minutes No. 14, Clause 3 of the Meeting of the Council of  
the Financial and Capital Market Commission)

# **Normative Regulations for the Establishment of the Internal Control System of Payment Institutions and Electronic Money Institutions**

*Issued in accordance with Section 48 Part two of  
the Law on Payment Service  
and Electronic Money*

## **I. General provisions**

1. "Normative Regulations for the Establishment of the Internal Control System of Payment Institutions and Electronic Money Institutions" (hereinafter referred to as – the Regulations) lay down minimum requirements for establishment practices of an effective internal control system, and shall be binding on the Latvian Republic licensed and registered payment institutions and electronic money institutions operating under the [Law on Payment Services and the Electronic Money](#) (hereinafter referred to as – the Institution). It is recommended to apply the principles of establishment of the internal control system specified in the Regulations to payment systems, if the requirements are related to the basic principles of their activities, as well as the scope, type, complexity and specificity of their activities.

2. When establishing an internal control system, an institution shall comply with the requirements of these Regulations in accordance with the scope, types, complexity and specificity of its activities, taking into account the risks associated with each area of activity, the institution's governance model, information technology and other factors which are essential to the achievement of the institution's operational objectives. A payment institution registered in the Republic of Latvia and an electronic money institution shall document and assess the application of the requirements of [Chapter XII](#) of these Regulations, taking into account the specifics of its activities.

3. Terms used in this Regulation:

3.1. employees – all employees of the institution who have an actual legal employment relationship with the institution, except for officials;

3.2. officials – members of the board and council of the institution (if such has been established);

3.3. compliance laws, rules and standards – laws and other legal acts governing the activities of an institution, standards established by self-regulatory authorities with respect to the activities of an institution, codes of professional conduct and ethics and other best practice standards related to the activities of an institution;

3.4. customers – a circle of persons who, taking into account the specifics of the activities of the institution, are holders of electronic money and users of payment services, as well as customers of the institution within the meaning of the [Law on Payment Services and Electronic Money](#);

3.5. customer funds – money received from payment service users and electronic money holders or another payment service provider for the execution of payments;

3.6. the use of other terms corresponds to the use of terms in the [Law on Payment Services and Electronic Money](#).

## **II. General requirements for establishment of the internal control system**

4. An institution shall organize its internal control system in such a way that the institution's officials have reasonable confidence that the institution's assets and customers' funds are secured against losses and unauthorised management and use, that operational risks are monitored and assessed on an ongoing basis and that the transactions are carried out in accordance with the procedures set in an institution and are properly recorded, and an institution operates soundly, prudently and effectively in full compliance with the requirements of laws and other legal acts.

5. The internal control system shall include appropriate policies and control procedures to manage the risks associated with the activities of an institution. An institution shall implement control procedures that ensure the effective protection of the assets of the institution and protection of customers' funds and the risk management by avoiding the establishment and maintenance of formal and cumbersome rules and procedures.

6. The officials of an institution shall be responsible for the establishment and effective functioning of the internal control system of an institution, taking into account the functions of the council and the board of an institution referred to in [Chapters X and XI](#) of these Regulations.

7. If an institution has not established the council, the duties of the council of an institution referred to in these Regulations shall be performed by the shareholders or members.

8. The core elements of the internal control system are:

8.1. setting the development strategy and activity planning for each year;

8.2. an organisational structure appropriate to the size and operational risks of the institution;

8.3. identification and management of all significant risks arising from the activities of the institution, incl. measurement, assessment and control;

8.4. appropriate accounting and management information system;

8.5. protection of assets, customers' funds and information systems;

8.6. improvement of the internal control system, compliance with changing operating conditions and evaluation of its efficiency;

8.7. management of outsourced services and representatives, where used by an institution;

## **III. Setting the development strategy and planning of the activities**

9. An institution shall develop and document its development strategy, specifying therein:

9.1 objectives of the activities, inter alia, shall determine the planned financial situation, types of activities, target markets, target customers;

9.2 risk strategy (policy), inter alia, shall identify the risks an institution is ready to take, tolerable risk level, actions for ensuring compliance with the tolerable risk level;

9.3. objectives in the field of liquidity management, considering the characteristic indices of the activities and financial situation of an institution, as well as the regulatory requirements;

9.4. capital adequacy maintenance strategy.

10. An institution shall develop the plan of activities for each year, specifying the financial situation of an institution planned for at least the following year, its market position, operational objectives during the respective period, types of activities and most typical transactions, potential risks and risk tolerance ratios, performance assessment criteria.

11. An institution shall establish and document procedures for the conduct and control of transactions. These control procedures shall at least entail the procedure for authorising the person concluding the transaction (inter alia, shall specify the documents required to be completed during the process of adoption of the decision until the approval of the performance of the transactions, and the officers or employees confirming the adoption of the respective decisions), the setting of restrictions to ensure the conformity of the transaction to the policy of an institution and compliance laws, rules and standards, as well as the procedure for the processing and control of the transaction. An institution shall ensure that officials and other employees involved in the conduct of those transactions are made aware of those procedures.

12. An institution shall establish and document procedures for establishing relationships with new customers and approve the form and content of documents to be completed when dealing with or on behalf of customers and third parties. An institution shall determine the information that it needs to receive about its customers and ensure that information is kept up to date. An Institution shall ensure the rights of persons to the personal data protection and confidentiality in accordance with the requirements of Regulation (EU) [2016/679](#) of the European Parliament and of the Council on the protection of individuals with regard to the processing of personal data and on the free movement of such data and repealing Directive [94/46/EC](#) (General Data Protection Regulation) by organizing meetings with customers and third partners, in correspondence with customers and third parties.

#### **IV. Organisational structure**

13. An institution shall ensure the appropriate organisation of its activities, inter alia, establish a transparent organisational structure appropriate to the size and operational risks of an institution, which shall be reviewed at least annually and updated as necessary.

14. An institution shall ensure that the composition of the Board and the Council, if any, are appropriately structured and balanced, taking into account the size, specificity, complexity and development strategy of an institution.

15. An institution documents its organisational structure, defining the duties (functions), powers and responsibilities of officials and employees in conducting and controlling transactions, defining and allocating responsibilities between departments and preparing general job descriptions (service instructions).

16. When documenting the organisational structure, the procedure for reporting and exchange of information within the institution shall be determined, inter alia, outlining who and when is obliged to provide and receive what type of information and which information is confidential and cannot be disclosed further.

17. When defining the duties of the officials and employees and granting powers thereto, the segregation of duties principle shall be observed, expressed as the segregation of such duties (functions), which, if combined, would enable an official or employee to entirely unilaterally carry out any transaction alone. The principle of segregation of duties covers at least the activities of approving, executing, valuing, comparing, storing and recording the transaction.

18. When documenting the granting of powers, the type of powers granted, the delegation rights of a person (specifying the position) which the powers have been granted to, delegation rights, as well as all restrictions for exercising granted powers, shall be specified. When granting powers to officials and employees, an institution shall ensure that the officials and employees are acquainted with the scope of authority granted to them.

19. All transactions shall be authorised by order or decision of the official or employee concerned in accordance with the levels of responsibility specified in the organisational structure.

#### **V. Personnel compliance, remuneration policies and corporate values**

20. An institution shall ensure that its officials and employees are informed about their duties (inter alia, with respect to risk identification and management), know the information related to their official duties and they have the appropriate qualification and sufficient experience. To ensure compliance of the employees, the institution shall:

20.1. develop and document personnel policy and procedures laying down at least such aspects as the procedure for the selection, hierarchical supervision and succession planning for employees in executive positions, requirements for the skills in various positions, criteria and procedure for the suitability assessment of potential officials and employees;

20.2 provide officials and employees information related to their official duties, for example, development strategy, operational plan for each year, corporate values, professional conduct and ethics standards, operational procedures, risk management policies and control procedures, compliance laws, rules and standards;

20.3. develop and document a professional training programme for the officials and employees aimed at preparing officials and employees for the fulfilment of the duties of the relevant position and continuously enhancing their knowledge, as well as include the procedure for informing officials and employees about changes in policies, procedures, compliance laws, rules and standards related to the fulfilment of official duties of the employees;

20.4. taking into account the scope, type, as well as the complexity and specificity of its activities, develop and document an appropriate remuneration system for officials and employees, inter alia, remuneration policy, ensuring that it does not depend solely on the achievement of short-term objectives (including short-term profit-making) and does not encourage the taking of risks which cannot be effectively managed by an institution, and is in the long-term interests of an institution. An institution shall develop and document appropriate remuneration policies and procedures, inter alia, determine the procedure for determination of remuneration and provide for adequate criteria for determination of the variable part of remuneration, which are commensurate with the assessment of the performance of the relevant official or employee, the overall operational assessment of an institution and the development strategy. An institution shall ensure that the amount of the variable part of remuneration paid to officials and employees is proportionate to the size of the fixed remuneration component.

21. An institution shall ensure that both the board and the council (if any) collectively possess sufficient experience and knowledge about all material activities and risks of an institution.

22. In order to ensure that each official has sufficient competence and skills to perform his or her duties in the board, the council and the committees (if any), an Institution shall ensure that each official has access to appropriate internal or external training or advice as necessary.

23. Officials of an institution shall devote sufficient time to the performance of their duties.

24. An institution shall set and document the corporate values of an institution, inter alia, shall determine high professional conduct and ethical standards to ensure that the officials and employees of an Institution perform their duties with the highest degree of integrity, are objective when performing their official duties and taking decisions, observe compliance laws, rules and standards, respect the confidentiality of information about transactions and customers and trade secret, including observe the basic principles of personal data protection, and their conduct and behaviour conforms to high ethical standards. It is especially important that standards address corruption, insider dealing and any other unlawful, unethical or questionable conduct, as well as mitigate risks pertaining to the operational activities and reputational risks.

25. An institution shall develop and document the overall policy and procedures for the governance of conflict of interest situations with respect to all employees and officials of an institution ensuring the timely identification and governance of actual or potential conflict of interest situations and prescribing the conduct for the prevention of conflict of interest situations, which might arise between the interests of the relevant persons and the interests of an institution, *inter alia*:

25.1. shall prevent the formation of situations, where the conflict of interest situation occurs or might occur, for example, by ensuring the appropriate distribution of duties among the employees and officials of an institution;

25.2. ensure that an official or other employee of the institution, in the performance of his or her duties, refrains from taking decisions on the institution's business or other professional activities within an institution if this person has or may have a conflict of interest situation, as well as ensures appropriate procedures for officials and employees to report to the board or council of an institution (if any) on transactions in which the person concerned directly or indirectly has or may have a conflict of interest situation;

25.3. shall ensure that the structural units, carrying out activities among which a conflict of interest situation occurs or might occur, are mutually independent, for example, certain information barriers, different organisational subordination.

26. An institution, when ensuring the governance of conflict of interest situations in an institution, shall take appropriate organisational and administrative measures preventing an adverse influence on the interests of the customers or potential customers.

27. An institution, taking into account the scope and complexity of its activities, provides the institution's officials and employees with the possibility for internal whistleblowing on actual or potential weaknesses in the internal control system, make proposals for their prevention thereof and report unlawful or unethical transactions, incl. conflict of interest situations. An institution shall establish and document appropriate procedures and make them available to officials and employees of an institution.

## **VI. Institutional risk management**

28. An institution shall develop, document and implement appropriate policies and procedures for identifying and managing material risks inherent to the activities of an institution, *inter alia*, for the measuring, assessing, controlling of risks and risk reporting.

29. An institution shall ensure that appropriate quantitative and qualitative criteria are used to identify material risks and that the results and conclusions of the assessment are substantiated and documented. Depending on the nature and type of the institution's activities, at least the following risks are assessed:

29.1. the risk associated with the protection of customers' funds;

29.2. counterparty risk;

29.3. credit risk;

29.4. operational risk;

29.5. operational compliance risk;

29.6. money laundering and terrorism and proliferation financing risk and sanctions risk;

29.7. risk of information technologies;

29.8. the risk of fraud regarding payments;

29.9. other material risks affecting the institution's operations, such as country risk, strategy risk, reputation risk, risks associated with the representatives and outsourcing, if an institution uses such services.

30. An institution shall ensure the integration of money laundering and terrorism and proliferation financing risk and sanctions risk into the risk management system of an institution, as well as shall ensure the management thereof in accordance with the requirements laid down in the [Law on the Prevention of Money Laundering and Terrorism and Proliferation Financing](#), the [Law on International Sanctions and National Sanctions of the Republic of Latvia](#), as well as the requirements specified in the normative regulations of the Financial and Capital Market Commission (hereinafter referred to as – the Commission) which prescribe the management of the risk of sanctions.

31. With respect to the risks identified by an institution as material for its activities, an institution shall develop, document and implement appropriate risk management policies and control procedures, specifying:

31.1. methods and regularity of risk measurement (for the risks which cannot be measured in quantitative figures, such as reputational risk, strategy risk) and assessment (for risks that can be measured in quantitative figures);

31.2. appropriate risk control procedures, inter alia, in accordance with the risk strategy of an institution, shall determine the restrictions and limits of maximum risk amount that can be tolerated, methods for hedging of risks, control procedures for mitigating the risks which cannot be measured using quantitative figures, as well as appropriate restrictions before engaging in new transactions;

31.3 Procedure under which the officials receive regular information about the risks inherent to the activities of an institution, the scale and trends, the impact of risks on the amount of the capital of an institution, as well as other information necessary for the decision-making;

31.4. regular monitoring of compliance with risk management policies and procedures and control of compliance with any established limits;

31.5 division of duties, powers and responsibilities within risk management.

32. An institution shall, on a regular basis, however at least on an annual basis, review and improve risk identification and management policies and procedures consistently with the changes to the activities of an institution and external circumstances affecting the activities of an institution. An institution shall assess its compliance with the provisions of risk identification and management policies and procedures, the adequacy and efficiency of these policies and procedures, as well as the appropriateness and efficiency of the measures taken by an institution to eliminate the deficiencies identified in the referred to policies and procedures.

33. An institution shall develop, document and implement a policy for the introduction of new payment services, which sets out the procedures and requirements to be followed when introducing new payment services, starting to offer existing payment services to new market segments or making material changes in the procedure for the provision of the existing payment services. An institution shall determine:

33.1. the definition of a new payment service;

33.2. definition or description classifying material changes in the procedure for the provision of the existing payment services;

33.3. the compliance of the new payment services, as well as the existing payment services, the procedure for the provision of which has been materially changed, with the risk strategy of an institution and the impact thereof on the overall risk profile of an institution;

33.4. an assessment of the level of training (including knowledge and skills) of officials and employees;

33.5. an assessment of the resources available to an institution (including their adequacy and conformity) for the introduction of new payment services or for making material changes in existing payment services;

33.6. the ability of an institution to comply with compliance laws, regulations and standards when introducing new payment services or making material changes to existing payment services.

34. An institution, that makes material changes in relation to its electronic money services (including issuance, distribution and redemption), shall comply with the requirements referred to in Paragraphs 33.2–33.6 of these Regulations.

## **VII. Organisation of accounting**

35. An institution shall establish and maintain an accounting system, taking into account the laws and other legal acts governing the organisation of accounting of an institution, by developing and documenting the accounting policy (specifying how various transactions are reflected in accounting) and procedures for the recording, control and assessment of reporting.

36. An institution shall ensure that all transactions are processed in a timely manner and that a balance sheet is prepared at the end of each cycle of activity.

## **VIII. Management information system**

37. An institution shall develop a management information system, which permits the users to understand and assess the financial standing of an institution on a timely basis, to effectively make decisions and to assess the consequences thereof, as well as to discover the failure to comply with control procedures on a timely basis. The officials and employees of an institution shall have timely access to accurate, complete, credible and appropriate information necessary for the performance of their official duties and decision taking, both under normal operational conditions and in a crisis situation.

38. Management information system shall at least entail:

38.1. current standing and performance results of an institution in comparison with the previous periods and indicators of the operational plan;

38.2. information on customers' funds;

38.3. analysis of the assets, liabilities and off-balance items, specifying how they are measured;

38.4. analysis of income and expenses, including the dependence thereof upon various classes of assets, liabilities and off-balance items;

38.5. an assessment of the compliance of the actual quantitative risks to the risk strategy of an institution and comparison with the prescribed restrictions and limits;

38.6. listing and analysis of cases of non-compliance with the adopted policies and procedures.

39. Information system shall ensure the provision of timely, accurate, complete, credible and appropriate information to external users (for example, the Commission, the Bank of Latvia, etc.) in accordance with the requirements of the applicable legal acts, both under normal operational conditions and in a crisis situation, within the term specified in the relevant legal act and upon request.

40. An institution shall ensure the availability of adequate resources for aggregating information related to risk management and the preparation and provision of management information and information to external users.

## **IX. Protection of assets, customers' funds and information systems**

41. An institution shall establish and document procedures for the protection of assets, customers' funds and information systems that:

41.1. ensure the preservation of the tangible and financial assets of an institution;

41.2. ensure the preservation of customers' funds;

41.3. prevent unauthorised direct or indirect (via documents) access of third parties to the assets of an institution and customers' funds, accounting, electronic communication system and other data of an institution;

41.4. ensure safe and sound functioning of information systems and the preservation of information (including restoration of information in extraordinary situations).

42. An institution shall organize the protection of information systems in accordance with the normative regulations of the Commission regarding the security requirements of information systems.

## **X. Functions of the council in the field of the internal control system**

43. The council of an institution (if any) shall control how the board of an institution ensures the establishment and effective functioning of the internal control system. When carrying out the control of the internal control system, the council of an institution shall:

43.1 divide the duties among the members of the council and principles for information exchange between the council and the board;

43.2. determine the duties of the members of the board (or control the fulfilment of the duties of the shareholders or members) and the procedure for the evaluation of the results of the activities of the board;

43.3. approve or accept the organisational structure of the institution for further submission to the shareholders or members of an institution for approval to ensure that duties and responsibilities are adequately defined;

43.4. approve and, if necessary, modify the risk management policies recommended by the board for both ongoing and planned transactions, including risk assessment and control procedures, authorisation procedures for such transactions, as well as setting restrictions regarding specific risks, request and receive information regarding material violations of the established restrictions;

43.5. control the establishment of an effective management information system;

43.6. control whether the internal audit service or an equivalent internal audit control function is clearly defined, has an appropriate position in the organisational structure of an institution and a particular role in the management process of an institution, whether qualified personnel is provided and whether they operate effectively;

43.7. regularly control the compliance of the internal control system with changes in the activities of an institution and external conditions affecting the activities of an institution;

43.8. review the internal audit service or equivalent internal audit functions, certified auditors, as well as of the Commission and other authorities for enhancement of the activities of an institution and shall control the prevention of the detected weaknesses;

43.9. determine the content, volume, format and frequency of reports it receives, as well as shall critically assess and, if necessary, dispute the truthfulness of such information.

44. An institution which has not established a council shall ensure the requirements referred to in this Chapter, subject to [Paragraph 7](#) of these Regulations.

## **XI. Functions of the board in the field of the internal control system**

45. The board of an institution shall be responsible for the establishment of the comprehensive internal control system, its implementation, management and enhancement in accordance with the strategy established by an institution. In the field of the establishment of internal control system, the board shall:

45.1. set qualitative and quantitative objectives for each area of activity of an institution in accordance with the strategy set by an institution;

- 45.2. develop an organisational structure with clearly defined powers and an effective division of responsibilities between officials and employees;
- 45.3. ensure appropriate qualification and sufficient experience of the personnel of an institution;
- 45.4. ensure the protection of the institution's assets and customers' funds;
- 45.5. ensure the identification, assessment and management of operational risks;
- 45.6. implement and manage a management information system that covers all activities of an institution;
- 45.7. set the principles for accounting and valuation of the assets, liabilities, off-balance claims and obligations, income and expenses;
- 45.8. put in place control mechanisms that ensure that all employees and officials of an institution comply with applicable laws and other legal acts, policies, plans, internal code of conduct and procedures approved by an institution;
- 45.9. ensure the implementation of measures to eliminate the deficiencies of the internal control system which have been discovered by the internal audit service or an equivalent internal audit function, a certified auditor, the Commission and other institutions;
- 45.10. at least once a year, provide the institution's board (if one has been established) with a report on the operation of the internal control system;
- 45.11. if the council of an institution has not been established, the report referred to in Paragraph 45.10 of these Regulations regarding the operation of the internal control system shall be submitted to the shareholders or participants at least once a year;
- 45.12. determine the content, volume, format and frequency of reports it receives, as well as shall critically assess and, if necessary, dispute the truthfulness of such information.

## **XII. Internal audit**

46. An institution shall establish an internal audit service or equivalent internal audit function (hereinafter referred to as – the internal audit) taking into account the scope, nature, complexity and specificity of an institution's activities. The role of internal audit is to carry out independent monitoring of the internal control system and to assess its effectiveness in assisting the institution's officials and employees in carrying out their duties more effectively.

47. The duties of the internal audit shall include:

- 47.1. assessment of effectiveness and results of the activities of an institution;
- 47.2. assessment of the compliance of all types of activities of an institution and the activities of the structural units with the strategy, plans, policies, procedures and requirements of external regulatory enactments;
- 47.3. verification of the accounting system;
- 47.4. evaluation of information systems;
- 47.5. verification of functioning of the internal control procedures;
- 47.6. verification of credibility and completeness of financial information, as well as the verification of the means, by which such information is identified, measured, classified and disclosed;
- 47.7. carrying out special verifications and investigations.

48. In order for the internal audit function to work effectively, an institution shall:

- 48.1. clearly define and document the powers of the internal audit activity;
- 48.2. separate the internal audit from the day-to-day operations and control functions, as well as from the determination of accounting and control procedures;
- 48.3. ensure free access to all documents, information and personnel for internal audit;

48.4. ensure that the internal audit employees has sufficient education and professional experience to consider that they are competent to perform their duties;

48.5. ensure direct contacts with the institution's council (if any) and the board for internal audit.

49. The shareholders or members of an institution shall approve the head of the internal audit, clearly stating and documenting its responsibilities, authority and procedure for the provision of reports. The head of the internal audit should be independent of the institution's board in making decisions and taking actions, for example, by ensuring its subordination to the institution's council (if one exists) or to shareholders or members if the council does not exist.

50. The internal audit activity shall be carried out in accordance with the operational plan approved by the institution's council (if any), which shall reflect:

50.1. areas of the activities to be verified during the reporting period, regularity of verifications and resources necessary for the performance of verifications;

50.2 risk identification and assessment methods for the areas to be verified, as well as criteria for the assessment of risk control procedures;

50.3. requirements for documentation of the results of verifications;

50.4. the procedures under which the results of verifications shall be submitted to the council of an institution (if such has been established) and the board, and the procedures for the verification of the implementation of recommendations.

51. If an institution has not established a council, its internal audit operational plan shall be approved by the shareholders or members.

52. The internal audit shall prepare reports on facts discovered as a result of each performed verification and weaknesses in the internal control framework, violations of policies and procedures, insufficiently identified or managed risks, and shall submit recommendations for solving the problems discovered. The internal audit shall ensure discussion of the facts discovered and opinions and recommendations prepared as a result of each performed verification at the relevant level of management, as well as shall perform the follow-up checks of the implementation of the recommendations made. The internal audit shall at least on an annual basis prepare the report on performed verifications and main problems discovered, expressing its view on the effectiveness of the internal control.

### **XIII. Final Provision**

53. An institution shall ensure that the requirements laid down in these Regulations are implemented not later than six months after the entry into force of these Regulations. An institution shall coordinate the implementation of the requirements of the rules after this deadline with the Commission.

Chairperson of the Financial and Capital Market Commission *S. Purgailė*