LATVIA: REVIEW OF THE INSURANCE SYSTEM

April 2016

OECD

REVIEW OF LATVIA
BY THE WORKING PARTY OF GOVERNMENTAL EXPERTS ON INSURANCE

This review of Latvia by the OECD Working Party of Governmental Experts on Insurance is part of a series of reviews of national policies undertaken for the OECD Insurance and Private Pensions Committee (IPPC). The IPPC was requested to examine Latvia's position with respect to core principles related to insurance systems.

The present report was finalised on the basis of information available in April 2016. It is released on the responsibility of the Secretary General of the OECD.

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1. Insurance system of Latvia

1.1 Overview of the insurance sector

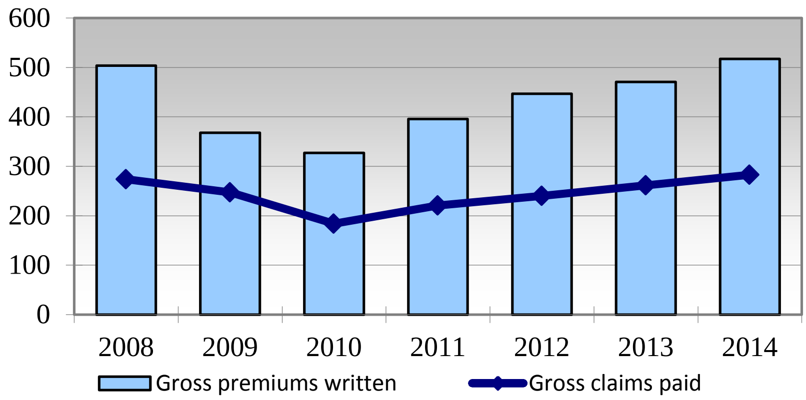
1. The Latvian insurance sector is small compared to other OECD countries in terms of assets of the overall financial system at 2.4% of GDP. The total gross premiums of Latvian insurance companies were EUR517 million in 2014 with a penetration of 2.1%, and density of USD315. Currently, the banking system has a large importance in the financial system but it is expected that assets of the insurance sector will grow substantially when pension savings that are accumulated in second pillar are released to buy annuities from life companies. There are no reinsurance undertakings in Latvia.

Table 1. Relative size of various types of financial institutions at end-2014 (% of GDP)

Financial Sector	Basis of calculation	Relative size
Banks	assets	128.1
Pension funds	net assets	9.5
Investment funds (except pension funds)	net assets	1.1
Investment firms	total assets	0.1
Non-life insurance	total assets	1.7
Life insurance	total assets	0.7

Source: Latvian authorities

Figure 1. Annual growth of gross premiums and gross claims (million EUR, %)



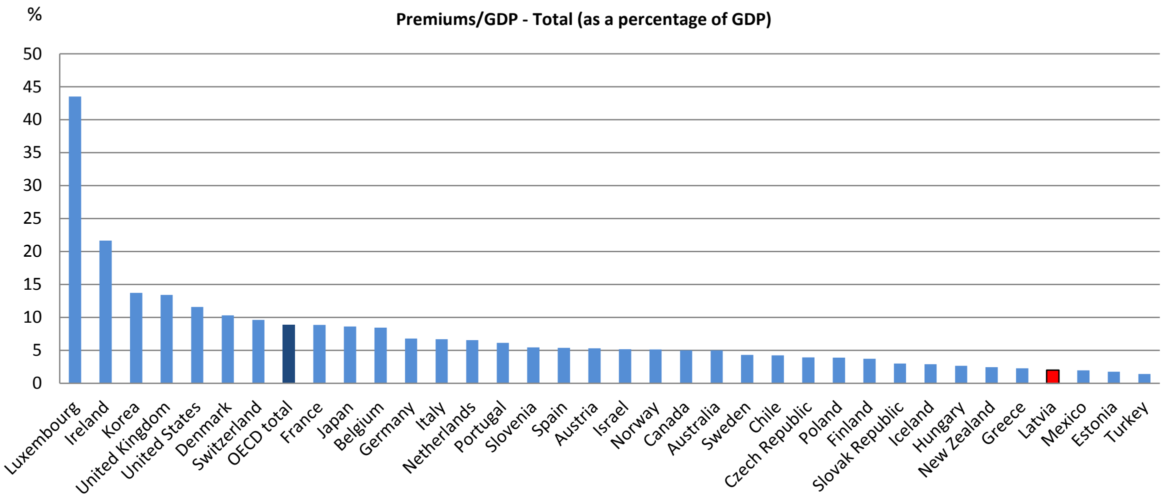
Source: Latvian authorities

Table 2. Gross premiums, penetration and annual growth rate of premiums (million EUR, %)

Year	Life sector			Non-life sector			Total	
	Premiums	Penetration (%)	Growth rate (%)	Premiums	Penetration (%)	Growth rate (%)	Premiums	Penetration (%)
2007	69	0.3		393	1.9		462	2.2
2008	67	0.3	-2.9	436	1.9	10.9	503	2.2
2009	58	0.3	-13.4	310	1.7	-28.9	368	2.0
2010	75	0.4	29.3	252	1.4	-18.7	327	1.8
2011	73	0.4	-2.7	323	1.6	28.2	396	1.9
2012	78	0.4	6.8	369	1.7	14.2	447	2.0
2013	89	0.4	14.1	382	2.3	1.6	471	2.0
2014	107	0.4	20.2	411	1.7	7.6	517	2.1

Source: Latvian authorities

Figure 2. Penetration in the OECD and Latvia, 2012[1]



Source: OECD Insurance Statistics 2013 and OECD Global Insurance Statistics.

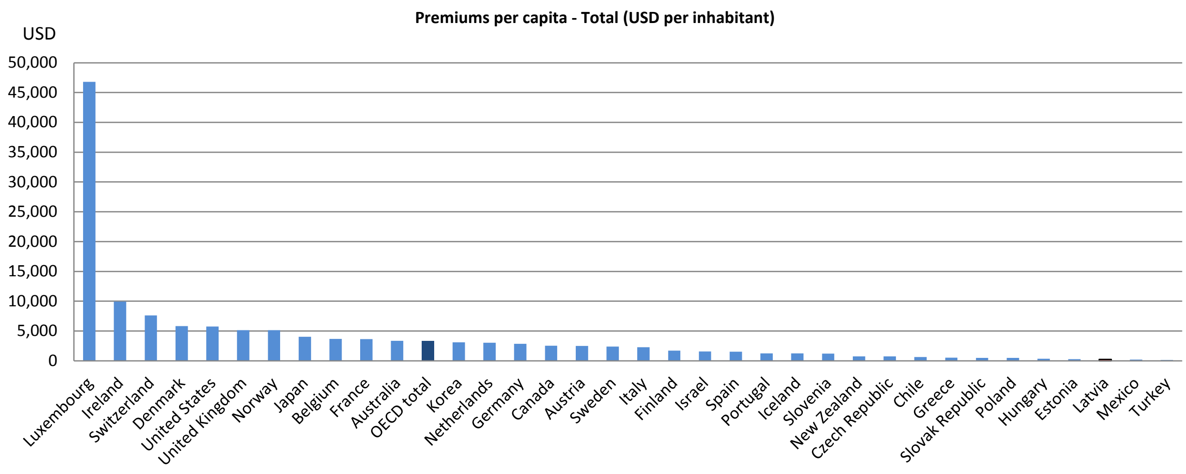
Table 3. Density (Gross premium/capita, US dollar)

Year	Life sector	Non-life sector	Total
2008	42	273	314
2009	37	197	234
2010	44	147	191
2011	46	202	247
2012	50	239	289
2013	60	258	318
2014	65	250	315

Source : Latvian authorities

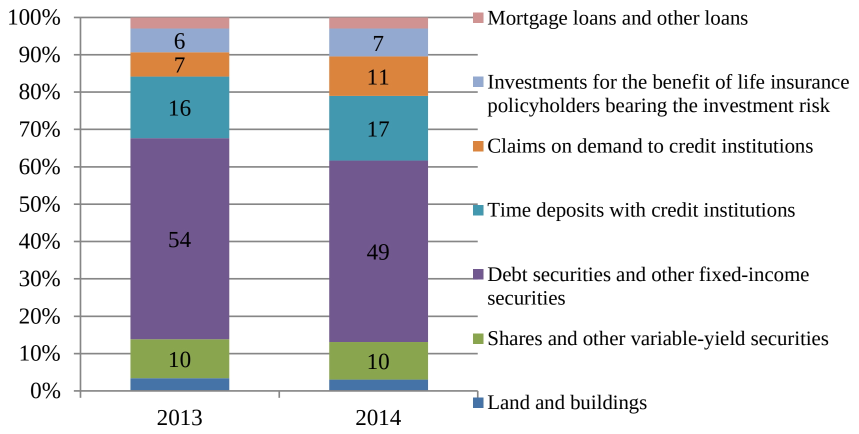
[1] The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Figure 3. Density in the OECD and Latvia, 2012



Source: OECD Insurance Statistics 2013 and OECD Global Insurance Statistics.

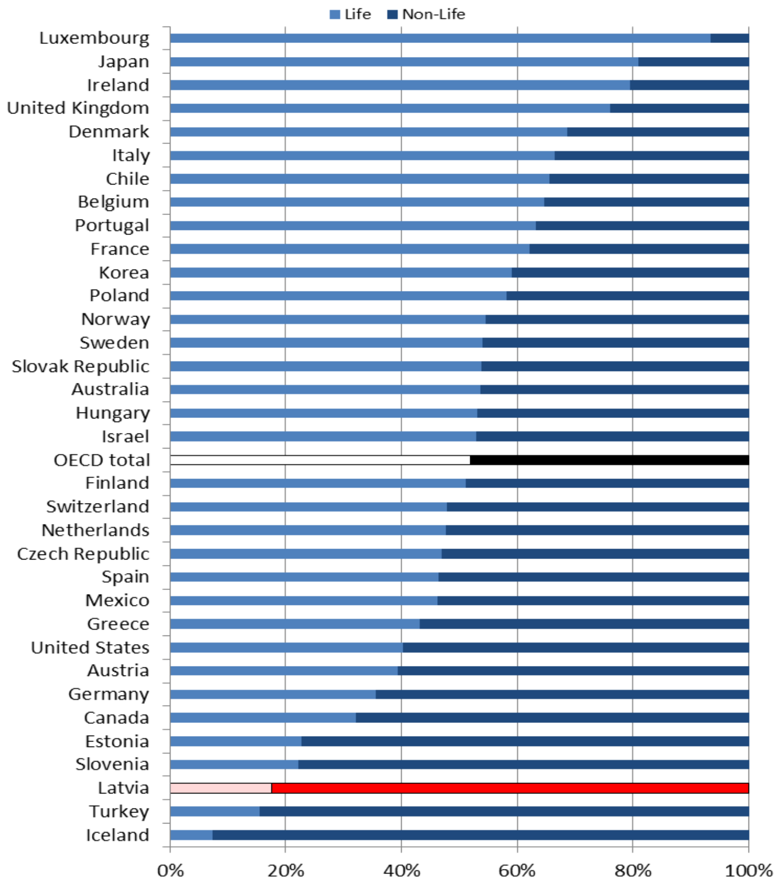
Table 4. Investments of insurers



Source : Latvian authorities

2. In the insurance market, 66.1% of the business is generated from the non-life sector. However, the life insurance market has grown as, in 1997, non-life insurance dominated the market by 88.1% of insurance business. Life insurance (with savings), accident and health insurance are still underdeveloped in Latvia.

Figure 4. Life and non-life insurance in selected OECD countries and Latvia, 2012



Note: Life insurance share is the ratio of gross life insurance premiums to total gross premiums. Data for Austria refer to gross premiums of direct business only. Data for Japan about total non-life gross premiums refer to 2011.

Source: OECD Insurance Statistics 2013 and OECD Global Insurance Statistics.

Table 5. Assets in the life and non-life sectors (Million EUR)

Year	Life sector		Non-life sector		Total	
	Total assets	No. of companies	Total assets	No. of companies	Total assets	No. of companies
2008	102	4	459	11	561	15
2009	112	4	399	10	511	14
2010	139	4	377	9	516	13
2011	113	3	395	9	508	12
2012	129	2	425	7	554	9
2013	136	2	395	5	531	7
2014	156	2	421	5	577	7

Source: Latvian authorities

3. The loss ratio improved from 2009-2012 in the non-life sector, especially in the motor third party liability (TPL) sector. The improvement in loss statistics was large enough to compensate for lower growth and pressure from competition in the non-life sector. Increases in loss ratio which have been observed in the last two years have been mostly driven by the increase in claims incurred.

4. The life sector has experienced large losses from investments in recent years. The introduction of higher capital charges in 2007 and the global financial crisis has exacerbated the loss ratio of life insurers. The equity market downturn has affected the unit-link policies severely, with many contracts being cancelled due to the short-term losses incurred.

Table 6. Loss and combined ratio of non-life insurers (%)

Year	Gross loss ratio	Gross combined ratio	Net combined ratio
2008	56.6	87.3	93.4
2009	72.2	112.8	96.0
2010	62.4	102.5	97.4
2011	66.1	101.5	110.7
2012	55.9	91.6	100.4
2013	56.1	90.1	98.2
2014	62.7	97.3	99.9

Source: Latvian authorities

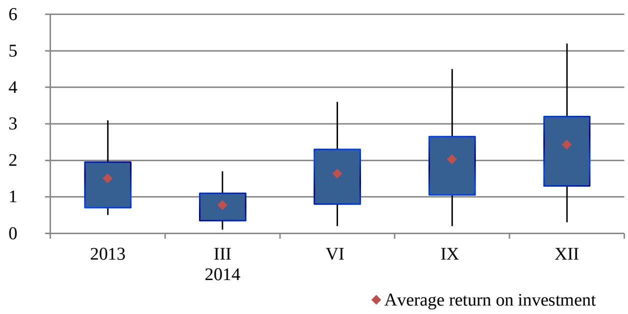
5. Through the years, the total net profit of non-life insurers has remained relatively high and the ROE (return on equity) has stayed above 5% (except for 2011). ROE has fluctuated widely (from -33% in 2011 to +27% in 2012) in the life sector due to market volatility. The total ROE for the life and non-life insurance sector in 2014 was 7.2%.

Table 7. Return on equity (%)

Year	Life sector	Non-life sector	Total
2008	-15.9	15.0	12.2
2009	0.1	10.6	9.4
2010	13.8	10.8	11.2
2011	-32.8	0.7	-1.7
2012	27.2	7.3	9.1
2013	-4.0	7.3	6.1
2014	19.5	5.4	7.2

Source : Latvian authorities

Table 8. Return on investments, %



Source: Latvian authorities

6. For life insurance companies, nearly half of their assets are placed in bonds. Until 2008, life insurers had nearly half of their assets in equity holding which decreased gradually since then. As for non-life companies, their assets are held in a more conservative portfolio, with a large share invested in bonds

and deposits. Investments are mainly European based. Reinsurance is purchased from abroad as there is no reinsurer based in Latvia.

7. In recent years, all insurers have been comfortably exceeding the available solvency margin with a substantial solvency margin. The average solvency margin of non-life insurance companies also exceeded the required solvency margin. The capital surplus is on an upward trend because insurers prefer to reserve profits instead of paying out dividends which are subject to the profit distribution tax.

Table 9. Total capital surplus (million EUR) and its percentage to policyholder liabilities (%)

Year	Life sector		Non-life sector	
	Owners' equity	% of policyholders' liabilities	Owners' equity	% of policyholders' liabilities
2008	15.3	20.9	149.5	57.2
2009	20.1	23.0	152.9	74.2
2010	23.3	20.9	158.0	86.5
2011	11.2	11.2	143.2	66.1
2012	14.2	12.9	143.8	59.1
2013	14.1	11.8	120.9	50.2
2014	17.5	12.7	118.7	45.1

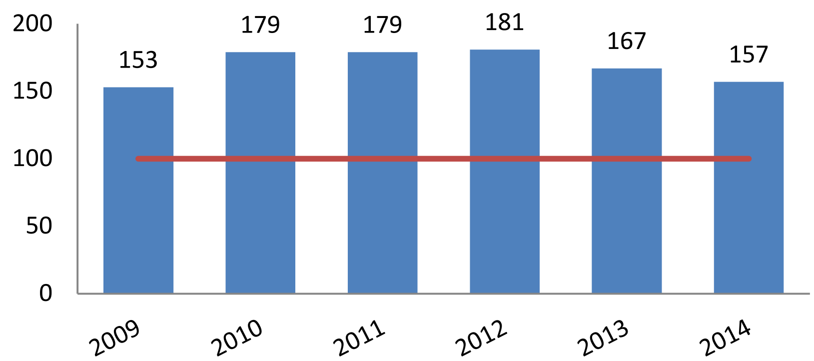
Source : Latvian authorities

Table 10. Capital adequacy of insurers (Million EUR)

	Life companies			Non-Life		
Year	Calculated solvency margin	Own funds	Surplus (%)	Calculated solvency margin	Own funds	Surplus (%)
2008	13.2	16.5	123.8	77.1	95.4	123.7
2009	13.1	20.9	159.5	66.5	100.9	151.7
2010	14.0	19.9	141.7	58.4	109.9	188.1
2011	10.5	10.5	99.6	59.3	114.2	192.6
2012	7.2	10.2	141.7	58.3	108.5	186.2
2013	7.5	13.7	181.9	55.3	90.1	163.0
2014	7.9	13.9	176.3	59.5	92.2	154.9

Source : Latvian authorities

Table 11. Solvency ratio (%)



Source : Latvian authorities

1.2 Evolution of the insurance industry

8. Developments in the Latvian insurance sector could be characterised by splitting it in several stages – a pre-crisis period where the insurance sector maintained a steady growth, a crisis period when the insurance market experienced a severe decline (written premiums shrank by more than 20% annually) and the return to growth in 2011 when insurance companies started to increase their activities mainly abroad. Gross premium per capita after the crisis continued to rise, and in 2014 reached EUR 260, even going slightly above the pre-crisis level.

9. At the end of 2014, there were two life insurance companies and five non-life insurance companies, as well as five branches of foreign life insurance companies and nine branches of non-life insurance companies operating in the insurance market. A number of market players have exited the market in the past five years, when in 2008 there were 27 insurers operating in the market (15 insurance companies and 12 branches of foreign insurers).

10. In 2014 the amount of gross premiums grew by 9.9% and totalled EUR 517 million, while gross claims paid grew by 8% amounting to EUR 283 million. Due to increase of incurred claims, the combined ratio deteriorated slightly for non-life insurance companies and stood at 99.9%.

11. Insurance companies' profits increased compared to previous year and was almost EUR 9.9 million (ROA 1.7% and ROE 7.2%) in 2014.

1.3 Products in the insurance sector

12. In terms of relatively new products, unit-link life products were introduced to the market in 2004, and legal expenses insurance products have been available since 2009.

13. There are two types of annuities offered in the market: 1) annuities with regular payouts starting when the beneficiary reaches the pension age but not earlier than age 55 and continuing until the beneficiary’s death or until the maturity date stated in the insurance contract, 2) annuities with a lump sum payout when the beneficiary reaches the pension age but not earlier than age 55.

Table 12. Marketshare of main products in non-life market (%)

Year	Land vehicle	Motor TPL	Property
2008	33.2%	28.8%	14.7%
2009	24.7%	32.3%	14.7%
2010	23.8%	32.4%	16.3%
2011	20.2%	38.4%	18.8%
2012	20.0%	37.9%	16.3%
2013	21.3%	40.0%	16.1%
2014	20.4%	36.3%	20.4%

Source: Latvian authorities

Table 13. Marketshare of main products in life market (%)

Year	Unit-link	Endowment	Annuities
2008	10.4%	38.1%	8.0%
2009	8.7%	51.6%	8.5%

2010	19.2%	48.5%	6.4%
2011	29.8%	66.1%	0.6%
2012	21.8%	74.0%	0.6%
2013	21.7%	74.6%	0.5%
2014	24.3%	72.6%	0.8%

Source: Latvian authorities

14. The marketshare of endowment products has been growing rapidly in recent years. In the aftermath of the financial crisis, policyholders of unit linked life assurance products experienced losses in Latvia, and as a result, products like endowment insurance experienced increased demand.

1.4 Competition in the insurance sector and entry/exit from the industry

15. Insurers may be a company in the form of a joint stock company, European company or a mutual cooperative insurance society. All insurers are privately owned. Three of seven insurers are part of an insurance group.

16. Over the last 10 years, there has been one entry in the insurance market. Joint stock insurance company (JSIC) Parex Dzīvība received licences for life assurance and accident insurance in 2007 which was subsequently renamed Citadele Life in 2010 after the failure of its parent Parex Bank.

17. Over the last 10 years, there have been seven exits from the insurance market:

i) JSIC Rīgas Apdrošināšanas sabiedrība by way of merger with JSIC Balta in 2004,

ii) two insurance companies were reorganised into a legal person that does not provide insurance – JSIC Salamandra-Baltik in 2004 and JSIC Nordens AS in 2006,

iii) the shareholder of RSK apdrošināšanas AS took a decision to terminate business in 2010,

iv) the Financial and Capital Market Commission (FCMC) decided to cancel all licences issued to provide insurance for JSIC LKB Life in 2012, to mutual insurance cooperative society Lauto klubs in 2012 and for JSIC Balva in 2013.

18. Over the last 10 years, six insurance companies exited the market as an insurance company and returned as a branch of an EU/EEA insurance company:

i) JSIC Seesam Life Latvia merged with Seesam Elukindlustuse Aktsiaselts in Estonia, and subsequently opened Seesam Life Insurance SE branch in Latvia in 2007 (renamed as Compensa Life Vienna Insurance Group SE Latvian Branch in 2009).

ii) JSIC Sampo Dzīvība merged with Sampo Elukindlustus in Estonia and subsequently opened SE Sampo Life Insurance Baltic branch in Latvia in 2006 (renamed as Mandatum Life Insurance Baltic SE branch in Latvia in 2010),

iii) JSIC If Latvia merged with If P&C Insurance AS in Estonia and then opened If P&C Insurance AS branch in Latvia in 2008,

iv) JSIC ERGO Latvija dzīvība merged with ERGO Lietuva gyvybės draudimas and ERGO Elukindlustuse AG establishing ERGO Life Insurance SE in Lithuania and then opened ERGO Life Insurance SE branch in Latvia in 2010,

v) JSIC Seesam Latvia merged with Seesam Insurance AS in Estonia and then opened Seesam Insurance AS branch in Latvia in 2011,

vi) AAS ERGO Latvia merged with ERGO Insurance SE in Estonia and then opened ERGO Insurance SE branch in Latvia in 2012.

Table 14. Insurance undertakings and their share of the insurance market in 2014

Number of insurance companies	7
Of which, number of non-life insurance companies	5
Of which, number of life insurance companies	2
Foreign branches	14
Of which, non-life branches	9
Of which, life branches	5

Source: Latvian authorities

Table 15. Home state of branches of foreign insurance undertakings in 2014

Number of foreign non-life insurance companies' branches	8
Estonia	4
France	2
Poland	1
Lithuania	1
Number of foreign life insurance companies' branches	5
Estonia	3
Poland	1
Lithuania	1

Source: Latvian authorities.

19. The Herfindahl index for the overall insurance market is low, while the index for the life and non-life segment is moderate.[2] Given the size of the market, the index indicates a good level of competition.

Table 16. Herfindahl index of the insurance market

Life	2050
Non-life	2405
Total	1603

Source: Latvian authorities

20. Acquisition of shares above certain thresholds is subject to the authorisation of the FCMC. The authorisation thresholds for acquisition are 20, 33 or 50% of voting rights or participation in its capital.

21. Though the process of changing insurance companies into foreign insurance company branches is still ongoing in Latvia, competition from branches with Nordic parents has maintained competitiveness in the market.

[2] A Herfindahl index between 1500 and 2500 is considered to be moderately concentrated and an index above 2500 to be highly concentrated according to the US Department of Justice. < http://www.justice.gov/atr/public/guidelines/hhi.html>

Table 17. Market concentration: marketshare of largest players (%)

Year	Life sector			Non-life sector		
	Biggest life insurers	2 biggest life insurers	3 biggest life insurers	Biggest non-life insurers	2 biggest non-life insurers	3 biggest non-life insurers
2008	53	98	99	22	39	53
2009	40	67	81	18	36	52
2010	39	59	77	19	32	44
2011	37	58	70	33	48	58
2012	34	56	68	32	46	56
2013	35	59	71	34	48	59
2014	33	56	69	43	58	71

Source: Latvian authorities

1.5 Foreign penetration

22. A large part of premiums (72%) in the insurance market are written by insurance companies, including subsidiaries of EEA insurance companies (42%). The average amount of premiums written by the EU member states insurers under the freedom to provide services in Latvia make up 4% of total premiums written in the insurance market.

23. At the end of 2014, insurance services providers from the EEA, by way of freedom of establishment, were 14 branches; and by way of freedom to provide services without establishment were 467.

Table 18. Shareholders of life insurance undertakings

Life insurance company	Main shareholders	Shareholder of main shareholder (if there is one)
AAS "SEB Dzīvības apdrošināšana"	SEB Trygg Liv Holding AB	
AAS "CBL Life"	Joint stock investment management company "CBL Asset Management"	Joint stock company "Citadele banka"

Source: Latvian authorities

Table 19. Shareholders of non-life insurance undertakings

Non-Life insurance company	Main shareholders	Shareholder of main shareholder (if there is one)
AAS "Balta"	Powszechny Zakład Ubezpieczeń Spółka Akcyjna	
AAS "Baltijas Apdrošināšanas Nams"	SIA "BAN Holdings"	
"BTA Insurance Company" SE	Gints Dandzbergs, Pauls Dandzbergs	
AAS "Baltikums"	Baltikums Bank AS, AS "BBG"	
AAS "Gjensidige Baltic"	Gjensidige Forsikring ASA	

Source: Latvian authorities

Table 20. Parents of life insurance branches in Latvia

Branch of Life EU/EEA Member State insurer	Life EU/EEA Member State insurer	Country
MetLife Towarzystwo Ubezpieczen na Zycie i Reasekuracji Spolka Akcyjna Latvia branch	METLIFE TUnŻiR S.A.	Poland
Mandatum Life Insurance Baltic SE Latvia branch	Mandatum Life Insurance Baltic SE	Estonia
Swedbank Life Insurance SE Latvia branch	Swedbank Life Insurance SE	Estonia
Compensa Life Vienna Insurance Group SE Latvia branch	Compensa Life Vienna Insurance Group SE	Estonia
ERGO Life Insurance SE Latvia branch	ERGO Life Insurance SE	Lithuania

Source: Latvian authorities

Table 21. Parents of non-life insurance branches in Latvia

Branch of Non-Life EU/EEA Member State insurer	Life EU/EEA Member State insurer	Country
Compagnie francaise d' assurance pour le commerce exterieur Latvijas filiāle	Compagnie francaise d' assurance pour le commerce exterieur	France
Swedbank P&C Insurance AS Latvia branch	Swedbank P&C Insurance AS	Estonia
GROUPAMA SA Latvia branch "GT BALTICS"	GROUPAMA SA	France
If P&C Insurance AS Latvia branch	If P&C Insurance AS	Estonia
Seesam Insurance AS Latvia branch	Seesam Insurance AS	Estonia
Compensa Towarzystwo Ubezpieczeń S.A. Vienna Insurance Group Latvia branch	Compensa Towarzystwo Ubezpieczeń S.A. Vienna Insurance Group	Poland
Uždaroji akcine bendrove draudimo kompanija "PZU Lietuva" Latvia branch	Uždaroji akcine bendrove draudimo kompanija "PZU Lietuva"	Lithuania
ERGO Insurance SE Latvia branch	ERGO Insurance SE	Estonia
If P&C Insurance Ltd (Publ) Latvia branch	If P&C Insurance Ltd (Publ)	Sweden

Source: Latvian authorities

1.6 Relationship of insurance with the pension system

24. The old-age pension system consists of a state-administered mandatory notional defined contribution (NDC) scheme, a mandatory funded scheme and voluntary private pensions. The NDC scheme is financed on a pay-as-you-go (PAYG) basis. Contributions paid into the scheme form pension capital that is accumulated notionally in individual accounts. The mandatory funded scheme is a fully funded defined contribution scheme, where contributions are invested in financial assets, mandatory for individuals born after 1 July 1971 who were under the age of 30 at the time of the reform. Those born between 2 July 1951 and 1 July 1971 can voluntarily participate in the funded scheme. Participants in the mandatory funded scheme can choose to invest their contributions in 23 different investment plans with three different risk profiles offered by seven different investment management companies.

25. At retirement, members can choose to have their accumulations added to those of their notional accounts and the pension is calculated as a life-time benefit in accordance with the rules used to calculate the NDC pension. A second option is to purchase a life-time annuity from an insurance company.

26. Participation in voluntary private pensions can be established directly through personal schemes offered by open private pension funds or through occupational schemes offered by the employer in open or closed funds.

1.7 Compulsory insurance

27. The major compulsory line of insurance is the compulsory civil liability insurance of owners of motor vehicles. The providers are five local insurance companies and six EU/EEA member states' insurer branches in Latvia.

- Tourism sector: tourism operators must provide guarantee of money deposited by a client, which usually comes in form of insurance policy, but can also be a bank guarantee.
- Construction: contractors must take out compulsory civil liability insurance policy. Construction specialists will be required to take out professional liability insurance policy.
- Defence: health insurance and accident insurance expenses are compensated for a specialised attaché, soldier or State administrative official (employee), while he or she is performing his or her duty in a foreign state, except for soldiers who carry out duties in a foreign state while participating in an international operation, military training, manoeuvres or on official journey.
- Mandatory State insurance is provided for reserve soldiers conscripted for military training. This insurance compensates a reserve soldier, who, if during the time of military training, has suffered health impairment.
- Civil servants (state officials): insurance of a state official when going on an official journey and insurance related to this official (employee).
- Health: medical institutions are required to have medical liability insurance. The license holder of a pharmacy shall insure all employees who work in a pharmacy or pharmacy branch.
- Environmental Protection and Regional Development: proposed amendments are being discussed to determine the need for civil insurance for public events. The Electronic Documents Law (Section 14) requires Trusted Certification Service Providers to insure their civil liability for the possible risk of losses associated with their activities. Activities with sources of ionising radiation are permissible if employees working with sources of ionising radiation are insured against accidents at work and occupational diseases, as well as civil liability insurance of operators.
- Interior System: officials with special service ranks of Ministry of the Interior institutions, who are retired from duty, have the right to receive paid health care if the official retired due to a health condition caused by injury or mutilation or other health impairment (except occupational disease) received in an accident during the fulfilment of service duties.

1.8 Distribution channels

28. The main distribution channels for sales of insurance products are direct sales and through insurance intermediaries. Direct sales are carried out by employees of insurance companies. There are three types of insurance intermediaries: an insurance agent, a tied insurance agent and an insurance broker.

- An insurance agent is a person who pursues insurance mediation on behalf of only one insurer. Credit institutions can also operate as insurance agents.
- A tied insurance agent is a person who, without receiving insurance premiums and other payments in accordance with insurance contract, pursues insurance mediation on behalf of and in

the interests of one or more insurers when the class of insurance provided by the insurers are not the same.

- An insurance broker is a person who pursues insurance and reinsurance mediation on behalf of and in the interests of a customer, on the basis of a fair analysis of products.

1.9 Reinsurer

At present, there is no reinsurance undertaking in Latvia, following the liquidation of Riga Re in 2009.

Table 22. Reinsurance ceded (percentage of insurance ceded to reinsurers)

Year	Non-life insurance	Life insurance	Total
2008	11.5%	18.5%	12.2%
2009	10.8%	1.3%	9.6%
2010	9.8%	1.2%	8.3%
2011	8.2%	0.6%	7.4%
2012	8.1%	0.6%	7.4%
2013	5.5%	0.5%	4.9%
2014	5.8%	0.4%	5.2%

Source: Latvian authorities.

1.10 Insurance associations

29. There are three insurance and insurance brokerage associations operating in Latvia – Latvian Insurers Association, Latvian Insurance Brokers Association and Latvian Professional Insurance Brokers Association.

30. The Latvian Insurers Association (LIA) represents the interests of the insurance industry in Latvia. LIA has as members 16 insurance companies and branches of foreign insurers (10 non-life and 6 life), which controls more than 99% of the total Latvian insurance market. LIA is also a member of Insurance Europe.

31. The Latvian Insurance Brokers Association (LIBA) has 45 members, comprising more than half of the insurance brokerage market. The purpose of LIBA is to enhance the development and qualitative growth of the insurance brokerage market as well as representing common interests.

32. Latvian Professional Insurance Brokers Association is a small professional insurance brokers association composed of only six members.

1.11 Risks of the insurance sector

33. The main challenge and risk for the insurance industry and markets is the implementation of Solvency II Directive requirements in legislation and regulation.

34. The survey on major catastrophic risks in Latvia, including major natural catastrophic risks, is organised by the State Civil Protection Plan. The most common natural catastrophe risks in Latvia are:

- Extreme temperatures (heat waves, drought, heavy snowfalls, hail and sleet): 2010;
- Storms: 1999, 2002, 2005;
- Floods (also caused by ice jams): 2010, 2013; and

- Forest fires (including peat bog fires, and grass fires) which occur annually.

35. There is a state-sponsored insurance scheme to provide state support for agriculture. It partly covers the expenses (50 percent of the insurance premium) for obtaining insurance coverage for cultivated plants and productive agricultural cattle, and promotes farmers' engagement in the agricultural sector's risk mitigation process.

36. The current legal framework and principles for disaster management are stipulated in the Civil Protection Law. State institutions analyse possible threats in the sector and annually submit proposals to the Ministry of Interior. Based on submitted proposals, the Ministry of Interior adjusts the disaster management measures defined in the State civil protection plan. National risk assessment for disaster risk management is carried out based on the European Commission's Risk assessment and mapping guidelines for disaster management[3].

37. The Law on Insurance Contracts sets out the conditions when an insurer is not liable for losses such as warfare, mass riots, radioactive contamination, radioactive pollution, natural disasters and other events specified in an insurance policy, unless stated otherwise in the policy/contract conditions.

2. Supervisory and Regulatory structure

38. Since Latvia joined the EU in 2004, its legal system has been harmonised with the EU including for regulation and supervision of the insurance system. Solvency II has been transposed into the Latvian legal framework. While preparing for the Solvency II regime, Latvia took part in Quantitative Impact Studies (QISs).

2.1 Policy and regulatory initiatives

Table 23. Regulatory initiatives

1998	Law on Insurance Companies and Supervision Thereof
	Law on Reinsurance
	Insurance Contract Law
2004	Law on the Compulsory Insurance against Civil Liability in Respect of Motor Vehicles
	The Cabinet of Minister Regulations No 1008 of 14 December 2004 "Regulations on the Amount and Procedure of Calculation of the Insurance Indemnity for Material Losses Caused to a Person"
May 2005	When Latvia became an EU Member, all the EU Directive provisions regarding the insurance sector were transposed into national legislation by amendments to the Law on Insurance Companies and Supervision Thereof, Insurance Contract Law and corresponding regulations.
2005	Activities of Insurance and Reinsurance Intermediaries Law
	The Cabinet of Minister Regulations No 195 of 22 March 2005 "Procedure of Establishment, Accrual and Administration of the Guarantee Fund for the Compulsory Third Party Liability Insurance for Owners of Inland Motor Vehicles"
	The Cabinet of Minister Regulations No 251 of 12 April 2005 "Regulations on Technical Examination of Motor Vehicles and Certification of Technical Experts"
	The Cabinet of Minister Regulations No 331 of 17 May 2005 "Regulations on the Amount and Procedure of Calculation of the Insurance Indemnity for Non-material Losses Caused to a Person"
2007	The Cabinet of Minister Regulations No 801 of 27 November 2007 "Regulations Regarding the Volume, Forms and Procedure for the Input, Exchange and Use of Data required for the Operation of Information System of Compulsory Third Party Liability Insurance for Owners of Inland Motor Vehicles"

3 . European Commission, staff working paper, 21/12/2010, SEC (2010) 1626 final.

2015	The Law on Insurance and Reinsurance[4] as well as secondary legislative acts transposing EU Solvency II regime[5] into national legislation have been adopted in 2015. The requirements of the Law on Insurance and Reinsurance will be applicable as of 1 January 2016 and will replace the requirements of the Law on Insurance Companies and Supervision Thereof and the Law on Reinsurance. The new requirements include: Solvency capital requirement and own funds; Calculation of technical provisions; System of governance; Supervisory reporting; Public disclosure; and Supervision of insurance and reinsurance undertakings in a group.

Source: OECD Secretariat

Table 24. Planned regulatory reforms

Scheduled date	Planned area of change
2016	Insurance Contract Law (replacing Insurance Contract Law currently in force) providing for the requirements for conclusion and termination of insurance contracts, the parties' rights and obligations and other provisions.

Source: Latvian authorities

39. The *Law on Insurance Companies and Supervision Thereof* determines the conditions relevant to the provision of insurance services, the legal status of these services and providers, and reorganisation and winding-up proceedings.

40. Insurance Contract Law applies to all insurance contracts but not to State social insurance and reinsurance. When concluding an insurance contract, parties to the contract are entitled to agree on the relevant jurisdiction of their contract unless otherwise provided by this Law. If the insurance contract concluded does not indicate the applicable law, this Law shall apply.

41. *Law on Reinsurance* determines the provision of reinsurance services. *Law on Compulsory Insurance against Civil Liability in Respect of Motor Vehicles* aims to protect the interests of third parties that have suffered in a road accident, and to regulate the legal relationship between motor vehicle owners, authorised users and insurers.

2.2 Regulatory objectives

42. The Law on the Financial and Capital Market Commission states that the FCMC is an independent/autonomous public institution that, in compliance with its goals and objectives, regulates and monitors the functioning of the financial and capital market and its participants (including insurers). Articles 5 and 6 of the Law on the FCMC state the following “the goal of the FCMC’s activities shall be to protect the interests of investors, depositors and the insured, and to promote the development and stability of the financial and capital market.”

43. The FCMC has the following functions[6]:

i) To issue binding rules, take decisions setting out requirements of financial and capital market participants, and calculation and reporting of their performance indicators[7];

[4] Available at: http://likumi.lv/ta/id/274969-apdrosinasanas-un-parapdrosinasanas-likums (Latvian only, English version currently not available).

[5] Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance.

[6] Cited from the unofficial translation provided by the FCMC for Article 6 of FCMC Law.

ii) To regulate activities of financial and capital market participants by requiring compliance with laws and regulations and rules and decisions adopted by the FCMC;

iii) To specify the qualification and conformity requirement for financial and capital market participants and their officials;

iv) To establish the procedure for licensing and registration of financial and capital market participants;

v) To collect and analyse information (data) relating to the financial and capital market and to publish it;

vi) To ensure the accumulation of funds in the Deposit Guarantee Fund, and Protection Fund for the Insured, their management and payment of compensation from these funds in accordance with the Deposit Guarantee Law and Law On Insurance Companies and Supervision Thereof;

vii) To ensure payment of compensations to investors in accordance with the Investor Protection Law;

viii) To analyse regulatory requirements pertaining to financial and capital market, and draft proposals for their improvement and harmonisation with that of the European Union;

ix) To engage in systemic studies, analysis and forecasting of the financial and capital market development;

x) To cooperate with foreign financial and capital market supervision authorities and participate in international organizations of the financial and capital market supervision institutions;

xi) To administer the financial stability fee in accordance with the regulatory requirements that govern the tax and fee area; and

xii) To control activities described in the laws and regulations governing the financial and capital market by limiting their provision to persons approved by the FCMC.

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[7] Performance indicators for life insurance companies are:

- Earned net premiums (in thousands of euro)
- Reinsurers' share in gross premiums written (%)
- Net claims incurred (in thousands of euro)
- Reinsurers' share in gross claims paid (%)
- Available solvency margin (in thousands of euro)
- Solvency ratio (%)
- Net technical provisions (in thousands of euro)
- Legitimate investments covering technical provisions (%)
- Return on investments (%)

Performance indicators for non-life insurance companies include performance indicators listed for life insurance companies plus the following:

- Market concentration (%)
- Reserve level (%)
- Loss ratio (%)
- Expenses ratio (%)
- Combined ratio (%)
- Operating ratio (%)

2.3 Governance and accountability of FSA

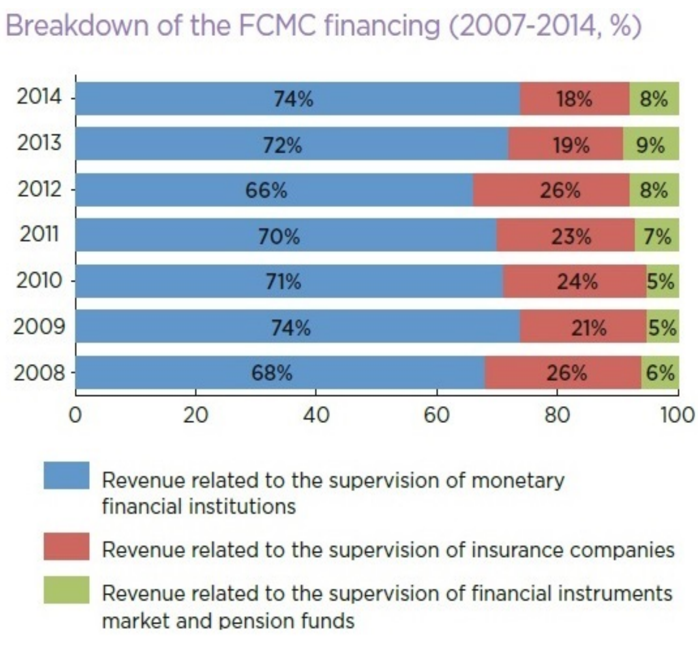
44. The FCMC is governed by its Board that is comprised of five members: the Chairperson of the FCMC, his/her Deputy and three members, who are also directors of FCMC's Departments. Parliament appoints the Chairperson and his/her Deputy for a period of six years upon a joint proposal of the Minister of Finance and the Governor of the Bank of Latvia.

45. A person may be appointed to the position of Chairperson, Deputy Chairperson or a Board member provided that he/she is competent in financial management, is of good repute; and has at least five years' experience in financial and capital markets. The position of Chairperson, Deputy Chairperson or Board member shall not be taken by a person who has a criminal record, irrespective of its annulment or removal, and has been deprived of the right to engage in a particular or any type of entrepreneurial activity.

46. The Parliament can dismiss the Chairperson or Deputy Chairperson from his/her position before the end of their terms only if an application on resignation is submitted by the respective person, a court judgment whereby the Chairperson or his/her Deputy is conviction of a criminal offence becomes effective, the Chairperson or Deputy Chairperson is not able to officiate for a period of six consecutive months due to illness or for any other reason, or an application submitted jointly by the Governor of the Bank of Latvia and the Minister of Finance on his/her early dismissal has been received.

47. The FCMC is empowered to make independent decisions within the limits of its authority, execute functions assigned to it by law, and be responsible for their execution, without interference. To take administrative action, the FCMC is not required to consult with another authority or a government minister. Law enforcement agencies may, however, ask for necessary information.

48. Regarding control of the FCMC's activities, the Law on the Financial and Capital Market Commission states that the FCMC must annually – but no later than 1 July – file with the Parliament and the Ministry of Finance a written report on its performance during the preceding year and full annual accounts audited by a sworn auditor.



Source: Latvian authorities

49. The Activities of the FCMC are fully financed from payments made by market participants. The basis of these payments and maximum percentages are set out in sectoral laws. The Board of the FCMC annually sets the percentage for payments of market participants taking into account the cost for supervising the respective sector and the sector's ability to ensure the necessary amount of financing. The annual budget of the FCMC is approved by the Board, before which a draft is reviewed by its Consultative Council although the Board makes the final decision.

50. The budget of the FCMC allows it to attract and retain experienced and qualified staff as well as to ensure necessary ongoing training. Salaries for staff are set taking into account the outcome of an independent research on the level of remuneration in the financial market, provided by a human resource management company. The Personnel Policy of the FCMC provides regular training of the employees. Each year the Personnel Division evaluates the training needs for employees and draws up the Training plan.

2.4 Compliance with international standards of supervision

51. An assessment of Latvia against the Insurance Core Principles (ICP) of the International Association of Insurance Supervisors (IAIS) was carried out in 2000 as part of the Financial Sector Assessment Programme (FSAP) which assessed Latvia as largely observant to all ICPs. Identified shortcomings, at the time, were the implementation of good corporate governance practices by insurers. Since 2000, Latvia has restructured its regulator, passed new insurance legislation and joined the EU which would have improved its position against ICPs further.

52. Latvia carried out a self-assessment against ICPs 1 and 2 on mandate and supervisory powers in 2011, and found itself to have observed both ICPs and relevant guidelines. Latvia also carried out a self-assessment against ICP 23 on group-wide supervision in 2012, and found that it had largely observed ICP 23.

2.5 Capital and surplus requirements

53. The solvency requirements of the insurance sector fully comply with EU requirements currently in force as stipulated in the EU Directives 73/239/EEC as regards the solvency margin requirements for non-life insurers, 2002/83/EC concerning life insurance, 2005/68/EC concerning reinsurance and 98/78/EC concerning insurance and reinsurance groups. The provisions of the Directives are transposed into the Law on Insurance Companies and Supervision Thereof, the Law on Reinsurance, as well as into the FCMC regulations regarding capital adequacy calculations for life, non-life, reinsurers and insurance groups.

54. The stability of an insurance company or a branch of a non-EU insurer is assessed based on the available solvency margin of the insurance or reinsurance company or the branch of the non-EU insurer, or the reinsurer shall be required to maintain the solvency margin and minimum size of guarantee fund. The required solvency margin may not be less than the minimum size of the guarantee fund.

55. The guarantee fund shall be the bigger of the following two figures:

1) one third of the estimated required solvency margin;

2) the minimum size of the guarantee fund.

56. The Law on Insurance and Reinsurance[8] as well as secondary legislative acts transposing EU Solvency II regime[9] into national legislation have been adopted in 2015. The requirements of the Law on

[8] Available at: http://likumi.lv/ta/id/274969-apdrosinasanas-un-parapdrosinasanas-likums (Latvian only, English version currently not available)

Insurance and Reinsurance will be applicable of 1 January 2016 and will replace the requirements of the Law on Insurance Companies and Supervision Thereof and the Law on Reinsurance.

57. Financial statements (consolidated financial statements) must be prepared on the basis of International Financial Reporting Standard (IFRS) issued by the IASB and its International Financial Reporting Interpretations Committee's standard interpretations that are endorsed by the European Commission and published in the Official Journal of the EU.

58. According to Paragraph 1 of Article 50 of the Law on Insurance Companies and Supervision Thereof, an insurance company or a branch of a non-EU insurer must carry out a critical situation analysis based on scenarios and documented at least once a year. Sensitivity tests shall be applied to assess the effect of an unfavourable change in one particular risk factor. Scenario tests shall be applied to assess the effect of simultaneous unfavourable changes in multiple risk factors when estimating the causes of exceptional but possible unfavourable future events or changes in market conditions.

59. According to the Law on Insurance Companies and Supervision Thereof, insurance services in Latvia may be provided through a commercial company in the form of a public limited liability company, a European commercial company, a mutual insurance co-operative society, or a branch of a foreign insurer, but only after obtaining a licence (issued by the FCMC) for the provision of insurance services.

2.6 Corporate governance

60. There are requirements in the Commercial Law and in the Law on Insurance Companies and Supervision Thereof on administrative, management, risk management, effective internal control, reporting procedures, internal reviews, fit and proper and minimum internal procedures.

61. The Law on Insurance Companies and Supervision Thereof states that an insurance company or a branch of a non-EU insurer shall ensure the setting up and operation of an efficient internal control system as well as constant supervision of the internal control system by the decision-making body. The decision-making body of the insurer shall be independent of the executive body. Monitoring of internal controls would ensure identification and management of all risks of the insurer, efficient protection for assets, provision of accurate financial and operational information to the management bodies of the insurer in a timely fashion, and compliance with relevant laws and regulatory requirements, and policy and procedures of the insurer.

2.7 Investment regulations

62. If an insurer's alternative investments are used to cover technical provisions, these investments have to comply with the requirements stated in the Law on Insurance Companies and Supervision Thereof (Articles 41 (3 and 4), 42, 42 and 43). There are restrictions and requirements only on insurers' assets and investments that form the technical provisions. The management of the insurance company or the branch of the non-EU insurer shall review its investment-making procedures and conditions at least once a year. Prior to transactions in derivative instruments, the management of the insurer shall formulate and approve procedures for the use of derivatives which are in line with the basic activity of insurer, and its investment-making procedures, including adequate risk management (Article 41 (1)).

63. In accordance with Paragraph 1 of Article 41 of the Law on Insurance Companies and Supervision Thereof, the investments of an insurer shall be safe, diverse, and liquid, ensure financial

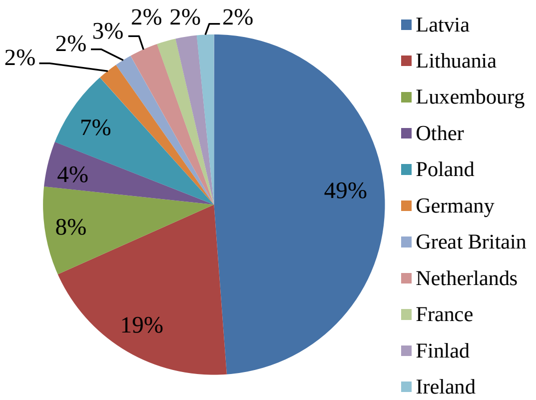
[9] Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance.

stability of the insurer, and guarantee the fulfilment of liabilities provided for in insurance contracts. The management of an insurer shall develop and approve procedures and conditions for the formation of investments of the insurer and is liable for compliance with such procedures and conditions. The following are the current investment regulations in relation to assets covering technical provisions:

- A maximum of 5% of technical provisions may be invested in equity securities and debt securities issued by one issuer (excludes debt securities issued by central and local government of Latvia, another EU or an OECD Member State);
- A maximum of 10% of technical provisions may be invested in mortgage bonds which have been issued in accordance with the Law on Mortgage Bonds or regulatory enactments of EU Member State and which have been issued by one issuer, and a maximum of 25% for all mortgage bonds;
- A maximum of 5% of technical provisions may be assigned to investment certificates of one investment fund registered in Latvia or another EU or an OECD Member State;
- A maximum of 10% of technical provisions may be assigned to one mortgage loan and a maximum of 25% for all mortgage loans ;
- A maximum of 10% of technical provisions may be invested in one piece of immovable property and a maximum of 25% for all buildings and land ;
- A maximum of 25% of technical provisions may be assigned to deposits with one credit institution.

64. The Law on Insurance Companies and Supervision Thereof states that an insurance company may not, directly or indirectly, issue loans for the acquisition of own shares or shares issued by persons linked to the insurance company, as well as to accept own shares for technical provisions (Article 46).

Figure 5. Total investment by region



Source: Latvian authorities

65. If an insurance company intends to outsource investments, there are requirements regarding outsource contracts and relevant outsourcing policies and procedures.

2.8 Group-wide supervision

66. Group solvency margin calculation is based on an aggregation and deduction method:

- When calculating adjusted solvency, no account shall be taken of capital eligible for the solvency margin arising out of reciprocal financing between the insurance undertaking, a reinsurance undertaking and/or a related undertaking, a participating undertaking, another related undertaking of any of its participating undertakings.

- Joining the Helsinki protocol[10] and being a member of the European Insurance and Occupational Pensions Authority (EIOPA) provides for the regular exchange of information among the supervisory authorities of the EU to ensure effective supervision of the groups and conglomerates.

67. Currently there is one domestic insurance group subject to group supervision carried out by the FCMC.

2.9 Early intervention and winding-up/insolvency

68. If there is a need for insurers to take corrective actions, the FCMC can apply one or several of the following tools or corrective actions:

i) arrange a meeting with an insurance company's management about future activities to improve the situation,

ii) send letter to the insurance company asking for certain measures to be taken,

iii) require reports more frequently, for example, monthly, from an insurer,

iv) use the tools or corrective actions envisaged in the Law on Insurance Companies and Supervision Thereof, for example:

- require a higher solvency margin,
- request the set-up of a particular type of technical provisions,
- request a change in the composition and structure of assets to cover technical provisions if the existing composition and structure of assets prejudice or may prejudice financial stability,
- request a plan for the improvement of financial conditions of an insurance company,
- apply security measures such as restricting the right of an insurance company to freely administer its assets and undertake new liabilities, or require prior compulsory co-ordination with the FCMC of all or part of payments,
- request the placement of reinsurance or the meeting of reinsurance obligations by the reinsurer's pledge of monies transferred to the possession of the insurance company in the amount of the technical provisions for reinsurance,
- require the insurance company to transfer all or part of concluded insurance contracts to another insurance undertaking which has agreed to accept such contracts,

v) suspend a licence, and

vi) cancel all insurance licences.

69. The insolvency and winding-up regime for insurers follows the general regulations laid down in the Insolvency Law and Commercial Law. Procedure for settling a creditors' claims, and duties of a liquidator are laid down in the Law on Insurance Companies and Supervision Thereof.

10 . Members of EIOPA agreed on a protocol relating to collaboration between supervisors for supervision of insurance groups <https://eiopa.europa.eu/fileadmin/tx_dam/files/Colleges/14.pdf>

2.10 Guarantee fund

70. The Fund for the Protection of the Insured (FPI) was created in 1999 to protect the interests of policyholders in case of an insurance company's insolvency. The assets of the FPI consist of 1% of the gross insurance premiums received from physical persons for the classes of insurance specified by law.

71. Only a policyholder who is a natural person may receive insurance indemnity in case of an insurer default:

i) for life insurance policies, except for insurance related to unit-linked life insurance contract, 100% of the insurance indemnity, but no more than EUR14,230 per insured person

ii) for other classes of insurance as established by law, 50% of the insurance indemnity, but no more than EUR2,850 per insured person.

72. FCMC collects premium for the FPI and carries out the payment of guaranteed insurance indemnity. The Consultative Council of the FCMC monitors collection of premiums for the FPI and the payment of guaranteed insurance indemnity. The guaranteed insurance indemnity is paid only after an insolvency procedure of an insurance company is initiated.

2.11 Complaint-handling and consultation process

73. In 2012, FCMC approved its internal complaints-handling procedure to review complaints received on financial and capital market participants' behaviour. The principal aim is to protect the interests of financial and capital market participants' clients, giving professional advice on complaints, as well as preventing financial and capital market participants from breaching laws and regulations. The FCMC's complaints-handling procedure:

1. describes how to deal with customer complaints, and submissions and proposals on financial and capital market participants' behaviour within the FCMC;
2. describes how to prepare FCMC's responses to complaints;
3. sets requirements for preparation and publication of a summary of complaints received, in order to ensure that the public is aware of the complaints FCMC has dealt with; and
4. exchanges information on consumer complaints with the Consumer Rights Protection Centre according to the cooperation agreement signed in 26.08.2010 between both authorities.

74. FCMC has to comply with the requirements set out in the Law on Submissions. The Law on Submissions prescribes the procedures by which a private person shall submit a document to state/public institutions, and how the State administration examines a document, which incorporates a request, a complaint, a proposal or a matter within the competence of the institution, and prescribes the procedures by which the institution shall receive visitors.

75. According to Paragraph 5, Section 5 of this Law, if the submission contains a complaint or dissatisfaction with an area which is in the competence of the state/public institution, or in relation to the action of an employee of the institution, the institution shall respond with considerations.

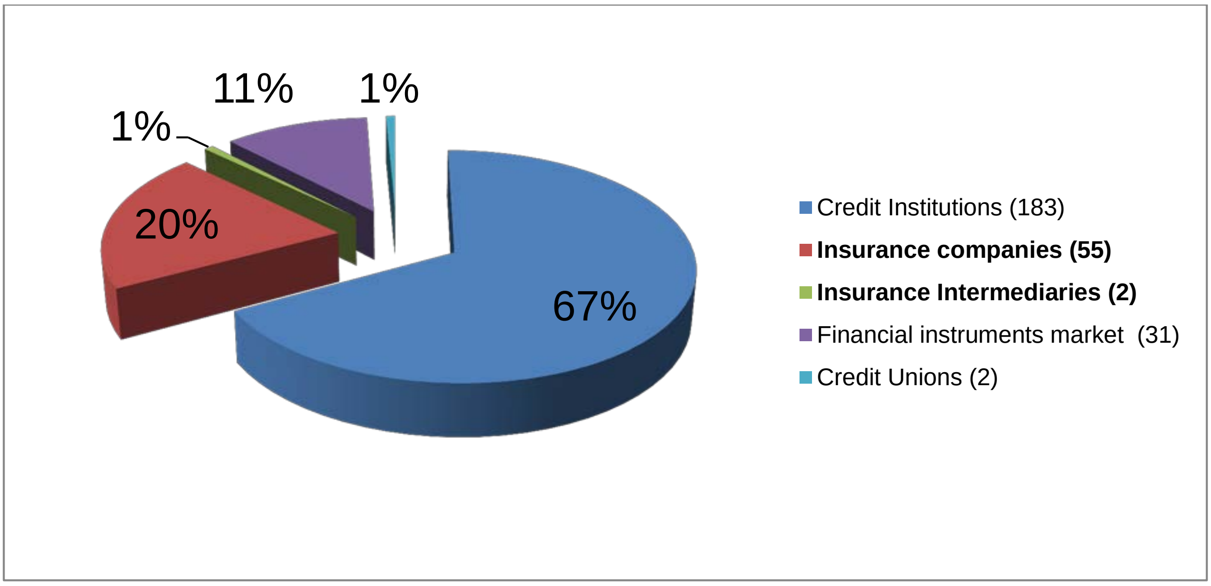
76. Additionally, Article 21 of the Law on the Financial and Capital Market Commission prescribes that the Consultative Council of the FCMC can review a complaint on FCMC's inspections upon a request from a financial and capital market participant's request.

Table 25. Number of insurance related complaints to the FSA, 2010-2014

Type of complaints	2010	2011	2012	2013	2014
Refusal of insurance indemnity payments	31	37	18	12	19
Amount of insurance indemnity payments	14	16	20	9	8
Decision delays	20	5	4	-	7
Delays in insurance indemnity payments	-	1	8	5	3
Complaints of unfounded subrogation	2	1	-	8	5
Others[11]	29	8	15	13	13
Total	**96**	**68**	**65**	**47**	**55**

Source: Latvian authorities

Table 26. Number of financial sector complaints in 2014



Source: Latvian authorities

2.12 Dispute settlement

77. According to Articles 1 and 29 of the Law on Insurance Companies and Supervision Thereof, an insurer or a branch has the duty to handle claims received in written form from the policyholder, the insured person or the person entitled to apply for indemnity under an insurance contract. The insurers must provide a written response 30 days after receiving the claim.

78. Depending on the particular dispute, consumer may seek help from the Consumer Rights Protection Centre, FCMC, Ombudsman of the Association of Latvian Insurers or by bringing an action to a civil court. The Consumer Rights Protection Centre, as provided by the Consumer Rights Protection Law, may, pursuant to the procedure provided by the law, demand that insurance service providers and authorised agents who violate the provisions of the Consumer Rights Protection Law or Unfair Commercial Practices Prohibition Law terminate the violation and refrain from violating the provisions.

[11] E.g., form of insurance indemnity payments, condition of insurance provisions, unfounded termination of the insurance contract, non-compliance with laws and regulations, information quality, reduced provisions etc.

2.13 Market conduct rules

79. The FCMC has the right to act if the insurance company or the branch of the non-EU insurer violates the laws or regulatory enactments governing commercial activity. According to Paragraph 1 of Section 29 of the Activities of Insurance and Reinsurance Intermediaries Law, an insurance intermediary shall comply with requirements for settlement of complaints against insurance intermediary.

80. The FCMC has internal standards for claims settlement. The FCMC, in every case, asks for an explanation from a market participant regarding the situation mentioned in the claim and after that prepares the answer to the claimant. If the market participant is found not to be in compliance with the requirements stated in the legislation, the following actions are taken: (a) if the non-compliance is insignificant, the market participant is requested to resolve it within a certain time period; and (b) if the legislation is breached several times or there are significant non-compliance, FCMC can take a decision imposing a sanction or restrictions on business if necessary to prevent repeated non-compliances.

81. The main consumer protection legal acts in Latvia are: the Consumer Rights Protection Law and the Unfair Commercial Practices Prohibition Law. All insurance intermediaries have to comply with the provisions of the Activities of Insurance and Reinsurance Intermediaries Law.

82. There are no specific rules, regulations and codes that apply to insurers regarding monitoring of intermediaries' performance on a continuous basis with the aim to enhance consumer protection. Paragraphs 1 and 4 of Section 10 of the Activities of Insurance and Reinsurance Intermediaries Law stipulate the requirements for establishment of an intermediary and procedures of insurance intermediaries. The intermediaries shall submit the procedures to the FCMC. According to Sections 10 and 13 of the Activities of Insurance and Reinsurance Intermediaries Law, insurance agents shall coordinate procedures with insurers.

83. According to Paragraph 1 of Section 29 of the Activities of Insurance and Reinsurance Intermediaries Law, intermediaries have a duty to ensure effective procedures for the examination of customer complaints. Written information regarding the procedures for the examination of complaints shall be freely available at the place of provision of insurance and reinsurance mediation and on the home page of the insurance and reinsurance intermediary, if such Internet home page is available. According to Paragraph 2 of Section 29 of the Activities of Insurance and Reinsurance Intermediaries Law, insurance and reinsurance intermediaries have a duty to provide a written reply to a customer complaint within one month from the day of the submission of the complaint or four months if an objective reason is provided.

84. The Law on Insurance Companies and Supervision Thereof states specific requirements regarding distribution and selling of insurance contracts with retention or possible over-insurance or under-insurance and unit-linked life contracts. According to Paragraph 2 of Article 7 of the Law on Insurance Companies and Supervision Thereof, an insurance undertaking may not disseminate false and misleading advertising of its activities.

2.14 Role of Actuary

85. According to Article 23 of the Law on Insurance Companies and Supervision Thereof, an insurance company or a branch of a non-EU insurer providing life insurance and any class of civil liability insurance shall employ a chief actuary whose minimum qualification shall be determined by FCMC.

86. The mentioned minimum qualification requirements are determined in FCMC regulations. A chief actuary must be a member of the professional actuarial association that is a member of the International Actuarial Association. According to the requirements of the International Actuarial Association every member association sets and enforces technical and ethical standards.

2.15 Taxation

87. According to Article 10 of the Law on personal income tax, insurance premiums with certain conditions are eligible as expenditure which can be deducted from the amount of annual taxable income. Furthermore, insurance compensation shall not be qualified as taxable income.

3. Market liberalisation in insurance and private pensions

3.1 Establishment of foreign insurers and private pensions

88. Latvia is open to establishment of foreign insurers by incorporation, the conditions for incorporation being the same for resident and non-resident investors.

89. According to Paragraph 2 of Article 11-2 of the Law on Insurance Companies and Supervision Thereof, the branch of the EU/EEA insurer may undertake insurance services in Latvia as soon as information from the home supervisory authority is received by FCMC or as soon as a two-month period expires.

90. A branch of a non-EU/EEA foreign insurer may launch operations in Latvia after obtaining a license issued by FCMC. According to Paragraph 5 of Article 10 of the Law on Insurance Companies and Supervision Thereof, FCMC shall take a decision on the application within a three-month period after the receipt of all the necessary documents prepared in compliance with the regulatory enactments. Administrative practices and criteria are identical to those applicable to domestically incorporated insurers.

91. There are no corporate tax differences between domestically incorporated insurers, and branches of foreign entities. The only difference in the tax treatment between domestically incorporated insurance companies and other companies is the possibility to reduce the taxable base for amounts transferred into technical reserves. Branches of foreign insurers are also allowed to create (attribute) such technical reserves.

92. Investors intending to acquire a holding (10, 20, 33 or 50%) of an insurer have to obtain the authorisation of FCMC, according to article 26 of the 1998 Law on Insurance Companies and Supervision Thereof. Investment funds and similar establishments are not entitled to acquire a qualifying holding in an insurance company.

93. According to article 31 (1) of the Law on Insurance Companies and Supervision Thereof, a branch of a non-EU/EEA insurer must place a security deposit of at least 25% of its guarantee fund with a credit institution in Latvia. The deposit must be freely available, it may not be encumbered, and its transfer is possible only with the permission of FCMC. The amount of the security deposit shall be taken into account in calculating its available solvency margin.

94. A foreign (re)insurer must register its representative office or permanent representative office in compliance with the Law on Foreign Investments in Latvia and, prior to launching business, shall notify FCMC in writing.

95. To receive a reinsurance licence, a non-EU/EEA reinsurer must submit an application to the FCMC. The FCMC shall examine the application within three months after receipt of the required documentation. The FCMC must, without delay, notify the reinsurer of the decision and issue the licence within three business days.

96. According to section 35 of the Activities of Insurance and Reinsurance Intermediaries Law, for an insurance and reinsurance intermediary of another EU/EEA member state to pursue insurance and

reinsurance intermediation in Latvia, the intermediary should obtain a notification from the home supervisor that they do not have objections against such activities.

97. By transposing the EU Directive on Solvency II into national legislation, there will not be any restrictions on the provision of services in Latvia by a non-EU reinsurer. The Law on Insurance and Reinsurance adopted on 18 June 2015 will be applicable from January 2016.

98. Insurance and reinsurance intermediaries from non-EU/EEA countries can provide insurance and reinsurance mediation services only through a branch. FCMC shall examine an application on whether to enter an insurance or reinsurance intermediary in the register of insurance and reinsurance intermediaries. The decision or refusal must be made and notified within 30 days after the receipt of the documents.

99. According to section 12-1-4 of the Activities of Insurance and Reinsurance Intermediaries Law, the equity capital of an insurance broker (a legal person) shall not be less than EUR15,000. For insurance brokers from OECD member states, the security deposit required by the law comprises 25% of the amount of equity capital required for local insurance brokers. The deposit shall be freely available, it may not be encumbered, and the transfer shall be possible only with the permission of FCMC.

100. According to the national legislation a pension fund of an EU/EEA member state may start accepting contributions for ensuring the supplementary retirement benefit from a sponsoring employer registered in Latvia, after the FCMC receives a notification from the home supervisor as stated in Paragraph 2 of Article 31 of the Law on Private Pension Funds.

101. Pension funds from non-EEA, OECD countries must be in the form of a joint stock company, which is registered in the Commercial Register and has been granted a licence for operations by the FCMC.

102. According to Article 6(1) of the Law on Private Pension Funds, founders of a closed pension fund shall be employers who establish and conclude a collective membership contract with a pension fund. Therefore, for founders of a closed pension funds, there are no requirements for the place of origin or type of legal form.

103. According to Article 6(2), founders of an open pension fund shall only be:

i) a bank that has received the licence for the operations of a credit institution in a EU or EEA member country, or is a member of the OECD; or

ii) a life insurance company that has received the licence for the provision of life insurance in a EU/EEA member country or is a member of the OECD.

3.2 Cross-border provision of insurance and private pension services

104. At the end of 2014, there were 467 providers of insurance services from EEA countries operating in Latvia under the “single passport” mechanism. An insurance company that intends to provide insurance services from an EU/EEA member states without opening a branch shall notify FCMC in writing.

105. Cross-border provision of insurance and reinsurance contracts by non-EEA foreign insurers is not permitted. Latvian residents, however, can acquire an insurance policy overseas upon their own initiative.

106. Insurance and reinsurance intermediation by non-EEA intermediaries cannot be made on a cross-border basis; establishment of a branch is required.

107. There are no restrictions regarding the currency denomination of insurance and reinsurance contracts concluded on a cross-border basis.

108. Private pension funds must have an establishment in Latvia for provision of services, and cross-border transactions are not permitted unless initiated by the beneficiary.

109. For private pensions, there are no restrictions regarding the currency denomination of pension contracts concluded on a cross-border basis. The open foreign currency position of a defined contribution scheme shall not exceed:

1. 10% of the assets of that pension scheme in a single foreign currency

2. 20% of the assets of that pension scheme in all foreign currencies

Table 27. Latvia's proposed reservations to the Codes of Liberalisation of Current Invisible Operations

D/2	Insurance relating to goods in international trade *Annex I to Annex A, Part 1, D/2* *Remark: the reservation, which includes the activity of promotion, applies only to compulsory third-party liability insurance for road vehicles by foreign insurers other than undertakings established in the EU.*
D/3	Life insurance *Annex 1 to Annex A, Part I, D/3, paragraphs 1 and 3* *Remarks:* *The reservation which includes the activity of promotion, does not apply to:* *i) insurance services provided by undertakings headquartered in the EU, or* *ii) if the policy has been taken out at the proposer's initiative.*
D/4	All other insurance *Annex I to Annex A, Part I, D4, paragraphs 4, 5 and 6.* *Remarks:* *The reservation which includes the activity of promotion, does not apply to:* *i) insurance services provided by undertakings headquartered in the EU, or* *ii) if the policy has been taken out at the proposer's initiative;*
D/7	Entities providing other insurance services *Annex I to Annex A, part IV, D/7* *Remark: the reservation which includes the activity of promotion applies only to intermediation services by services providers other than undertakings established in the EU.*
D/8	Private Pensions *Annex I to Annex A, part IV, D/8* *Remark: the reservation which includes the activity of promotion, applies only to private pension services provided in Latvia by non-resident service providers other than undertakings established in the EU, except if the policy has been taken out at the proposer's initiative.*

3.2 Trade Agreements

110. Latvia is a member of the WTO and EU with commitments under GATS and EU trade agreements. Under GATS, Latvia has undertaken specific commitments in the financial services sector with national treatment and several unbound limitations on market access with exceptions on pension fund management[12].

111. Under FTA's of the EU, there are 7 agreements that include financial services covering also insurance services and pension fund management (with Albania, Montenegro, Mexico, Chile, Korea, Former Yugoslav Republic of Macedonia, and with the Caribbean Forum of African, Caribbean and Pacific (ACP) States (Cariforum) (EPA).

4. Compliance with OECD Legal Instruments on Insurance

112. Latvia provided a self-assessment of its implementation of insurance-related instruments in its Initial Memorandum. Latvia's positions on insurance-related instruments appear satisfactory and do not raise any particular issues. In particular, Latvia has taken a number of actions to improve their financial education regime.

4.1 Recommendation of the Council on Good Practices for Mitigating and Financing Catastrophic Risks

113. Latvia accepts this recommendation.

114. The framework and principles for disaster risk management are stipulated in the Civil Protection Law. State institutions analyse the possible threats and annually submit proposals to the Ministry of Interior in areas of their responsibilities. Based on submitted proposals, the Ministry of Interior adjusts disaster risk management measures defined in the State civil protection plan.

115. Based on the guidelines set by the European Commission, risk assessment and mapping for disaster management is carried out. The Governmental Regulation No 1644 "Procedures by which Funds from the Budget Programme Funds for Unforeseen Events shall be Requested and Used" prescribes the procedures by which ministries, State institutions and local governments request funds for compensation of losses caused by disasters and other unforeseen events. The National Law on Insurance Contracts sets out the condition that an insurer is not liable for losses such as warfare, mass riots, radioactive contamination, radioactive pollution, natural disasters and other events specified in the insurance policy.

4.2 Recommendation of the Council on Good Practices for Enhanced Risk Awareness and Education on Insurance Issues

116. Latvia accepts this recommendation.

117. Issues related to financial education, particularly insurance issues, are discussed through the subjects "Social Sciences" in primary education (ISCED-2) and "Economics" in secondary education (ISCED-3).

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[12] The GATS' schedule of commitments of Latvia indicates that the exception for pension fund management is related to pension fund management provided by the state monopoly, the State Treasury. However, the state monopoly of pension fund management was disbanded in 2007 freed to private pension fund manager, and thus this exception is no longer applicable.

118. FCMC launched the educational website CLIENT SCHOOL on 1 March 2011, where clients can obtain detailed information and descriptions of the main financial products including insurance products. The CLIENT SCHOOL allows all clients to assess potential risks that may arise and to evaluate their readiness to bear risks.

119. In addition, FCMC plans to develop CLIENT ABC, where comprehensive clarifications will be provided to clients with different levels of knowledge regarding risks in different periods of life and appropriate insurance products.

120. Information for consumers can be found in a special section of the website of the LIA. Along with an introduction to insurance, it provides descriptions on several of the main non-life and life insurance products as well as explaining options for tax allowances and rebates. The LIA has posted parts of booklet "How insurance works" by *Insurance Europe* on the website of the LIA describing the basic principles and benefits of insurance, defining which risks are insurable, and introducing consumers to the importance of regulatory environment and the principles of premium calculation, as well as a link to the CLIENT SCHOOL website.

121. The LIA cooperates with the Consumer Rights Protection Centre in providing information about handling and settlement of consumer complaints. The LIA provides information to consumers about where they can receive help when there is incomprehension, disagreements and other issues with the contract.

122. The FCMC, together with its strategic partners on financial literacy, developed and agreed on the National Strategy for Financial Literacy of Latvian population 2014-2020 which will provide a unified strategic approach gradually improving the level of financial literacy. The strategy will focus on three main priorities: (1) tradition of financial planning and provisioning, (2) integrity of the financial services' environment, and (3) sustainability and development of the society finance. The Strategy was approved at the end of February 2014. The first National Survey on Financial Literacy based on OECD INFE Core Questionnaire was conducted by the FCMC in July, 2014.

4.3 Recommendation of the Council on Guidelines on Insurer Governance

123. Latvia accepts this recommendation.

124. General rules on the governance of insurers, including fit and proper requirements, are laid down in the Law on Insurance Companies and Supervision Thereof. FCMC's Regulations for Establishing the Internal Control System provide detailed requirements regarding the establishment of an internal control system, strategy, organisational structure, business ethics, a remuneration system, risk management, information system, functions of a management board and a supervisory board, as well as risk control, compliance and internal audit functions and fit and proper requirements.

125. In addition, FCMC's Regulations on Core Principles of Remuneration Policies prescribes core principles on remuneration policies, governance, performance assessment and disclosure of information on remuneration policy and has to be applied at all levels of positions who affect the institution's risk profile. Core Principles of Remuneration Policies also determine measures for preventing conflicts of interest. There is also the FCMC's Minimum Requirements Regarding the Qualification of a Chief Actuary.

126. According to FCMC's reporting regulations, the annual report of an insurance undertaking, among others, shall include a description on risk management goals and policy, information on the price, credit, liquidity and cash flow risk management of an insurer, recommendations on profit distribution, amount of dividends or covering of losses, and notification confirming the responsibility of management. In addition, the quarterly public reports should disclose the following information: financial position and activity results, financial activity indicators, risk analysis, specifying the types of risks, risk occurrence

reason, risk management and control and whether and how reinsurance, derivatives and alternative risk transfer or replacement mechanisms are applied in the risk management, the management and administration.

127. The basic requirements and responsibilities of the management and supervisory boards of joint-stock companies are stated in the Commercial Law.

128. The Law on Sworn Auditors lays down detailed requirements regarding qualification standards, independence, professional ethics, and rights and responsibilities of sworn (external) auditors.

129. The FCMC is currently working on a draft guideline on the system of governance which will be in line with EIOPA's Guidelines of System of Governance (EIOPA-CP- 13/08) and will cover different governance requirements (*e.g*., administrative, management and/or supervisory body, organisational and operational structure, key functions, decision-making and documentation of decisions, internal review of the system of governance, policies, contingency plans), fit and proper requirements (including policies and procedures, outsourcing of key functions), risk management issues (including the role of administrative, management or supervisory body in risk management, risk management policy and function, underwriting and reserving risk, operational risk, asset-liability management, investment risk, liquidity risk, risk-mitigation and risk management policy), the "prudent person" principle, own fund requirements (including the capital management policy), internal controls (including monitoring and reporting), internal audit function, actuarial function and outsourcing requirements.

4.4 Recommendation of the Council on the Establishment of a Check-List of Criteria to define Terrorism for the Purpose of Compensation

130. Latvia accepts this recommendation.

131. In Latvia, terrorism risk insurance is not compulsory. The Law on Insurance Contract states risks excluded from the scope of insurance (insurer shall not be liable for losses incurred due to war, riot, radioactive contamination, radioactive pollution, natural catastrophes and similar events stated in the insurance policy, unless otherwise stated by the insurance contract).

132. Additionally parties to the insurance contract may specify other excluded risks in the insurance contract. The vast majority of insurers have used this possibility and do not insure terrorism risk. The entities define terrorism broadly, in line with the definition provided in Criminal Law and that of the Recommendation. According to Article 88 of the Criminal Law, terrorism is defined as actions causing explosion or fire, use of nuclear, chemical, biological, bacteriological, toxic or other weapons of mass destruction, mass poisoning, or spreading of epidemics and epizootic diseases, kidnapping and hostage taking, seizure of aircrafts, vehicles or vessels and other actions taken with the purpose to intimidate inhabitants or coerce the state, its institutions or international organizations to act or to refrain from acting, or harm the interests of the state, its inhabitants or international organizations.

4.5 Recommendation of the Council on Good Practices for Insurance Claim Management

133. Latvia accepts this recommendation.

134. Claim processing and settlement requirements, including the terms for claim processing and settlement are laid down in the Insurance Contract Law. According to the Law on Insurance Companies and Supervision Thereof, an insurer is obliged to formulate, in writing, internal claim procedures, and comply with them.

135. As regards fraud detection and prevention, the Cabinet of Ministers Regulation on unusual transaction indicator lists the procedure for reporting unusual and suspicious transactions, establishes unusual transaction indicators, and approves the form of the report.

4.6 Recommendation of the Council on Assessment of Reinsurance Companies

136. Latvia accepts this recommendation.

137. As laid down in the Law on Reinsurance, a reinsurance company shall prepare an annual report in compliance with the Law on Accounting and regulations of FCMC. According to the FCMC's reporting regulations, the annual report of reinsurance companies, among others, shall include:

– developments and financial position of the reinsurer (group) in the accounting year;

– forecast of the reinsurer (group) for at least one year explaining every significant condition and risk;

– acquisition of own stock/shares;

– information regarding the most important events if such have occurred after the end of the accounting year;

– if use of financial instruments has materially influenced assets, liabilities, capital and reserves and results of activity, it shall be provided with:

- a description on risk management goals and policy including reference on the planned transaction types that for which it is planned to use hedging accounting;
- Information on price, credit, liquidity and cash flow risk management of an insurer.

4.7 Recommendation of the Council concerning a Common Classification of the Classes of Insurance Recognised by the Supervisory Authorities of the Member Countries

138. Latvia accepts this recommendation.

139. Classification of insurance classes is laid down in the Law on Insurance Companies and Supervision Thereof, and used mainly for licensing purposes and generally corresponding to the Recommendation.

140. According to Article 12, Paragraph one of the Law on Insurance Companies and Supervision Thereof, FCMC shall issue licences for the following classes of insurance:

1) accident insurance;
2) health (sickness) insurance;
3) land vehicle (except railway rolling stock) insurance;
4) railway rolling stock insurance;
5) aircraft insurance;
6) ship insurance;
7) goods in transit insurance;
8) insurance of property against fire and natural elements (damages to property, other than the property referred to in Paragraph one, Clauses 3, 4, 5, 6 and 7 of this Article) caused by fire, explosion, nuclear energy, earth subsidence, etc.;
9) insurance of property against other damage to property (damages to property, other than the property referred to in Clauses 3, 4, 5, 6 and 7 of this Article, caused by hail, frost, theft, etc., except those referred to in Clause 8 of this Article);
10) motor vehicle third party liability insurance;

11) aircraft ownership liability insurance;
12) ship ownership liability insurance;
13) general liability insurance;
14) credit insurance;
15) surety ship insurance;
16) insurance against miscellaneous financial losses;
17) legal expenses insurance;
18) assistance insurance;
19) life assurance.

141. According to Article 8, Paragraph 3 of the Law on Insurance Companies and Supervision Thereof, an insurance company or a branch of a non-EU/EEA insurer that has obtained a life assurance licence shall calculate insurance premiums or other amounts under insurance contracts by actuarial mathematical methods.

4.8 Recommendation of the Council concerning Institutional Co-operation between Authorities of Member Countries Responsible for Supervision of Private Insurance

142. Latvia accepts this recommendation.

143. According to Article 7 of the Law on the Financial and Capital Market Commission, FCMC has powers to cooperate with foreign financial and capital market supervision authorities and, upon mutual consent, exchange information necessary to execute its functions set forth by law.

144. The Law On Insurance Companies and Supervision Thereof provides that the FCMC is entitled to enter into agreements on information exchange with foreign supervisory authorities if the regulatory enactments of this foreign country stipulate liability equal to that specified in regulatory enactments of Latvia and are not permitted to disclose the information without the prior consent of FCMC. Such information shall be solely used for the supervision of financial and capital market participants and the performance of functions prescribed by the Law (such as licensing and supervision of insurers, etc.). The relevant foreign authorities are entitled to disclose the information received only when prior written consent is obtained from FCMC and solely for the purpose for which such consent was given. The FCMC is entitled to use information received from foreign supervisory authorities solely for the performance of its supervisory functions.

145. When signing agreements, the priority is given to those countries, with which Latvian insurance undertakings have established cross-border activities as well as to those countries where the EIOPA (or previously – CEIOPS) initiated signing of multilateral EU agreements.

146. The FCMC has entered into the following Memorandums of Understanding on information exchange and cooperation with foreign supervisory authorities:

1) Agreement on additional cooperation between the Banks of Lithuania and the Financial and Capital Market Commission of Latvia on supervision of cross-border insurance undertakings;

2) Agreement on additional cooperation between Financial and Capital Market Commission of the Republic of Latvia and the Financial Supervisory Authority of the Republic of Estonia on supervision of cross-border insurance undertakings;

3) Agreement of Mutual Co-operation with the Estonian Insurance Supervisory Authority and the State Insurance Supervisory of Lithuania;

4) Memorandum of Understanding between the Financial and Capital Market Commission of the Republic of Latvia and the Bundesaufsichtsamt für das Versicherungswesen of Germany regarding Insurance Regulatory Cooperation;

5) Memorandum of Understanding between the Financial and Capital Market Commission of Latvia and the Insurance Supervisory Authority of Finland;

6) Memorandum of Understanding between the Financial and Capital Market Commission and the Danish Financial Supervisory Authority;

7) Memorandum of Understanding regarding Mutual Co-operation and Exchange of Information in the Field of Insurance Supervision between the Financial and Capital Market Commission (Latvia) and the National Commissions for the State Regulation of Financial Services Markets (Ukraine);

8) Memorandum of Understanding between the Insurance Supervisory Authority of the Republic of Latvia as a Member of CEIOPS and the Insurance Supervisory Authority of Switzerland regarding Co-operation and Exchange of Information;

9) Multilateral Memorandum of Understanding on supervisory cooperation and exchange of information by and among the Bermuda Monetary Authority and the EEA supervisory authorities competent for insurance sector supervision.

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