FINANCIAL SUPERVISION AUTHORITY YEARBOOK
2008

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I. Address of the Chairman of the Management Board

Dear Reader,

Year 2008 will most certainly go into the history books: the global financial and economic crisis has undoubtedly had a substantial effect on current and future developments in Estonia's economy and financial sector. While the crisis has had a significant effect on all three levels – the state, local companies as well as individuals –, it is my pleasure to state that we have so far managed to avoid the collapse of financial services providers and the utilization of taxpayers' monies for ensuring the stability of market participants and the financial system. Still, significant effects of the crisis include the reduced value of investments as well as the escalating price of loan money. Offering of loans is directly influenced by strains on capital markets, marginal trust between banks as well as partly rational and partly emotional revaluation of accepted risks. This does not contribute to the improvement of our economic climate. In 2008, the financial sector as a whole experienced an escalation of risks.

Super-high-speed increase in banks' loan portfolios ended already in summer 2007. Today we can already speak of the decrease in banks' consolidated loan portfolio. Year 2008 was also characterized by a significant change in banks' market shares to the prejudice of two major banks. Our banking sector as a whole was characterized by a relatively rapid growth in overdue loans. The percentage of overdue loans is relatively higher in smaller banks and in smaller foreign branches. Delays in payments have become more frequent in all client groups, i.e. we do not speak about a few clients with problems; this is rather the effect caused by reversing economic cycle. Interests on arrears and credit losses are expected to experience a continuous increase. Still, banks have established adequate capital buffers and they are able to establish provisions for covering overdue loans four times as big as they currently have without any further need for supplementary capital. The profitability of banks has decreased less than expected due to extraordinary incomes.

In 2008, we focused more than ever on the analysis of banks' credit and liquidity risks; besides additional analysis, we also focused more on making various strength and stress tests addressing both credit institutions and insurance companies.

The integration of our financial markets with Scandinavian markets and the cross-border nature of the global financial crisis force us to cooperate actively with our colleagues from the Swedish Financial Supervisory Authority as well as from other Baltic countries. During these past two years, our collaboration with neighbors has developed from *ad hoc* cooperation projects towards so-called supervisory cooperation colleges which cover the whole spectrum of supervisory activities pursuant to multilateral agreements. The work of these colleges is planned long ahead, based on joint risk assessments. The efficiency and rapid development of the Financial Supervision Authority in exercising risk-based supervision as well as in relation with international collaboration was ranked high by both the IMF audit on the Estonia's financial stability framework and the Moneyval audit on the efficiency of anti-money laundering.

In order to reinforce the framework for crisis management, we signed an agreement with the Bank of Estonia and the Ministry of Finance, specifying the precise role of each institution and laying down collaboration mechanisms for preventing crisis situations and, if necessary, for managing these situations.

We continue to contribute to the promotion of consumer education and financial literacy. We upgrade our consumer education portal www.minuraha.ee on a daily basis in order to bring complex financial issues closer to people and to make them more understandable to consumers. We have translated our consumer education portal also into Russian, trying thus to provide balanced and objective information also to those Estonian citizens whose native language is other than Estonian. The attendance of this portal doubled in 2008; thus, we can see the genuine interest and need of consumers to rely on profound knowledge in the present situation.

I would like to thank all my colleagues and collaboration partners for their good work. I wish you good luck in managing this difficult economic situation.

Yours sincerely,

Raul Malmstein
Chairman of the Management Board

2. Confirmation of the Financial Supervision Authority's Management Board

In Tallinn, 13 March 2009

This Annual Report was prepared by the Management Board of the Financial Supervision Authority and is submitted for approval to the Supervisory Board of the Financial Supervision Authority. The Annual Report is presented to the *Riigikogu*.

This Annual Report includes the following documents of the Financial Supervision Authority:

Management Report on pages 5–37;
Annual Report of Revenues and Expenditures on pages 38–42;
Balance Sheet on page 43;
Auditor's Report on page 44.

The Management Board of the Financial Supervision Authority confirms that all facts presented in the Annual Report are correct and that the Annual Report of Revenues and Expenditures of the Financial Supervision Authority is in conformity with the Financial Supervision Authority Act and the applied accounting policies.

Raul Malmstein | Kilvar Kessler | Andres Kurgpõld | Kaido Tropp

3. Financial Supervision Authority's Management Report

3.1. Short description of the Financial Supervision Authority

The Financial Supervision Authority is a financial supervision agency with autonomous competence and a separate budget, conducting financial supervision in the name of the state and being independent in its activities and decisions.

The Financial Supervision Authority aims at contributing to the stability of companies offering financial services and the quality of these services, and thereby supporting the creditworthiness and stability of Estonian monetary system. The goal of financial supervision is to ensure the ability of financial institutions to perform their obligations in respect of clients, i.e. to pay out deposits, insurance losses or accumulated pensions, etc. In addition, an important task of the Financial Supervision Authority is to contribute to the effectiveness of Estonia's financial sector, to help preventing systemic risks and avoiding the abuse of the financial sector for criminal purposes. One of the tasks of the Financial Supervision Authority is to identify the risks in respect of consumers and to provide them information and support in choosing financial services. Work aimed at reducing systematic risks and preventing the abuse of the financial sector for criminal purposes is also of major importance.

Riigikogu adopted the Financial Supervision Authority Act on 9 May 2001 and the united supervisory authority commenced its activities on 1 January 2002. The Financial Supervision Authority joined the functions of the Banking Supervision Authority which operated at the Bank of Estonia, as well as the Insurance Supervisory Authority and the Securities Inspectorate which operated under the Ministry of Finance.

The Financial Supervision Authority's activities are planned and its management is controlled by the Supervisory Board. The Supervisory Board consists of six members; two of them are members by virtue of office and four are appointed members. One-half of the appointed members are appointed and removed by the Government of the Republic on the proposal of the Minister of Finance and one-half by the Board of the Bank of Estonia on the proposal of the President of the Bank of Estonia. Minister of Finance is acting as the Chairman of the Supervisory Board by virtue of office.

The Financial Supervision Authority's strategy for 2007–2010 sets the following main objectives for the Authority's activities: to improve cross-border supervisory capabilities; to increase the share of preventive supervisory methods; to raise the awareness level of financial services customers; to promote an open communication and working culture and to increase the effectiveness and minimize red tape through ensuring the competiveness of Estonia's financial sector at the international level.

3.2. Management and organization

3.2.1. Activities of the Supervisory Board

Members of the Supervisory Board

As at 31 December 2008, the Supervisory Board of the Financial Supervision Authority included:

Chairman:

- **Ivari Padar,** Minister of Finance

Members:

- **Andres Lipstok,** President of the Bank of Estonia
- **Matti Klaar,** Honorary Swiss Consul in Estonia, insurance expert
- **Ruut Mägi,** Auditing expert
- **Andres Sutt,** Vice-President of the Bank of Estonia
- **Veiko Tali,** Deputy Secretary-General for Financial and Tax Policies at the Ministry of Finance

Resolutions of the Supervisory Board

In 2007, the Supervisory Board held four ordinary meetings.

The Supervisory Board approved the 2008 Annual Report and the operational profit of the financial year within the amount of 3,060,000 kroons which was transferred to the budgetary reserve in order to ensure the sustainability of the institution.

The 2009 budget of the Financial Supervision Authority in the amount of 71,639,000 kroons was approved and a proposal presented to the Minister of Finance for setting the 2009 rates for the supervisory fee shares calculated on the basis of assets. Taking into account the low level of financial markets, the Supervisory Board followed the prudence principle in establishing the budget.

While planning the activities of the Financial Supervision Authority, the Supervisory Board focused especially on comprehensive analysis of the situation caused by the global financial crisis, on the necessity to plan potential preventive measures and thus also on the importance of operative exchange of day-to-day supervisory information with the supervisory authorities of other countries. It also focused on the need to reinforce the assessment of various risks. The Supervisory Board considered it essential to continue participating in the work of various EU working groups.

3.2.2. Activities of the Management Board

Members of the Management Board

As at 31 December 2008, the Management Board of the Financial Supervision Authority included:

Chairman:
Raul Malmstein (appointed as from 16 January 2006);

Members:
- **Kilvar Kessler** (appointed as from 1 January 2008)
- **Andres Kurgpõld** (appointed for the third term of office as from 1 January 2008)
- **Kaido Tropp** (appointed for the third term of office as from 1 January 2008)

The term of office is four years for the Chairman of the Management Board and three years for a member.

Resolutions of the Management Board

In 2008, the Management Board held 48 meetings and adopted 130 administrative decisions.

In 2008, the Management Board focused especially on the issues of liquidity risk and credit risk and on analyzing the effects of the global financial crisis. In addition, the Management Board participated in drafting legal framework for regulating national financial crisis.

Another priority was to introduce to market participants the MiFID framework (the Markets in Financial Instruments Directive of the EU) and to address the issues related to the implementation of good governance.

Due to changes in the economic environment, it was necessary to focus more on protecting the interests of holders of investment and pension funds' units, including on the adherence to the equal treatment principle. The Management Board continued to focus on raising the awareness of financial services customers, both via the targeted website and respective advisory guidelines.

Members of the Management Board – areas of responsibility

Raul Malmstein, the Chairman of the Management Board, is responsible for strategy development, organizing the general management and activities of the Management Board, ensuring effective functioning of all supervisory activities and coordinating them, coordinating institutional development and national cooperation, coordinating international and public relations and international cooperation, organizing internal audit, organizing staff training and ensuring the functioning of internal communication.

His direct area of responsibility covers the following positions:
- Assistant to the Chairman
- Head of Communications
- Head of Human Resources and Training
- Coordinator of International Cooperation
- Internal Auditor
- Consumer Education Specialist

Kilvar Kessler, the member of the Management Board, is responsible for the functioning of Market Supervision and Enforcement Division and Legal Department, including for coordinating the supervision of securities market and coordinating and preparing, if necessary, regulatory legal issues, developing the regulative environment of the financial sector, developing statements on financial and supervisory policies within his area of responsibility or together with other members of the Management Board, and directing international cooperation in his area of responsibility.

His direct area of responsibility covers the following divisions:
- Market Supervision and Enforcement Division
- Legal Department

Andres Kurgpõld, the member of the Management Board, is responsible for the functioning and development of Prudential Supervision, including for the supervision of credit institutions, insurers, investment firms and other supervised financial institutions, focusing on the monitoring of risks of supervised entities, their solvency and other prudential aspects. He is responsible for the process of market entry and market departure and ensuring that managers and shareholders are fit and proper. His area of responsibility covers also the process and development of regular reporting as well as international cooperation in his area of responsibility.

His direct area of responsibility covers the following divisions:
- Prudential Supervision Division
- Prudential Policy and Financial Reporting Division

Kaido Tropp, the member of the Management Board, is responsible for the functioning and development of Business Conduct Supervision Division and Administrative Services Department, including for the supervision of financial services, developing the regulative environment of the financial sector as well as statements on financial and supervisory policies in his area of responsibility, organizing the notification procedures in case of cross-border services, the process of anti-money laundering and prevention of terrorist financing, budgetary process of the Authority, functioning and development of administrative services, developing and implementing IT security procedures and ensuring international cooperation in his area of responsibility.

His direct area of responsibility covers the following divisions:
- Business Conduct Supervision Division
- Administrative Services Department

3.2.3. Organizational development, personnel policy and training

The Financial Supervision Authority values the principles of open organization; thus, the objective of the Authority's personnel policy is to ensure high supervisory standards through competent and motivated employees as well as an open working culture. The Authority has developed its recruitment and training policies and its motivation system, based on fair compensation for work.

In 2008, the Financial Supervision Authority performed the mapping of existing positions, describing main tasks related to various positions, replaceability of staff, workload of key personnel, as well as identifying priority areas for the Financial Supervision Authority that have not yet been covered.

68 positions out of 70 positions created in the Financial Supervision Authority were staffed as at 31 December 2008. Employment contracts had been temporarily suspended with 3 employees for the duration of parental leave, and 1 person was working at the CEBS (Committee of European Banking Supervisors) Secretariat. Based on the situation on financial markets and pursuant to indications from the IMF Financial Sector Assessment Program (FSAP), the Supervisory Board of the Financial Supervision Authority adopted a decision at the end of 2008 to increase the number on positions by 5 (up to 75 positions) as from 1 January 2009.

In 2008, the Financial Supervision Authority witnessed the arrival of 7 new employees and the departure of 3 employees. 2 internship contracts were signed for summer 2008. Internship program allows the Financial Supervision Authority to use students e.g. for carrying out various studies, creating thus its potential future employees.

There were 43 women and 25 men employed in the Financial Supervision Authority at the end of 2008. The average age of employees was 35 years. The core staff includes financial analysts, risk managers and lawyers. All employees are with higher education qualifications. As at the end of 2008, 10 employees were enrolled in the Master's Study Program and 3 in the Doctoral Study Program.

The Financial Supervision Authority as an organization values competence, openness and decisiveness. In order to increase the openness and effectiveness of the Authority and based on good administrative practices, the research centre Klaster performed an opinion survey in 2008, encompassing market participants in the Estonia's financial sector. The aim of the survey was to get a feedback on the level of satisfaction with the Authority's work and the competence of its employees. Results of this survey are available on the Financial Supervision Authority's website: http://www.fi.ee/failid/Turuosaliste_arvamusuuring.pdf. The competence of employees and the work of the Financial Supervision Authority were ranked high by market participants. Market participants emphasized the competence and relative openness of the Authority's employees in comparison with supervisors from other Baltic countries with whom many market participants had had contacts during their work assignments. The Financial Supervision Authority and its employees were generally regarded as competent, objective and open for communication.

The Financial Supervision Authority regards highly its employees, offering them motivating compensation packages, praising the best ones and investing in the training and professional development of its employees. The wage policy of the Financial Supervision Authority is based on the principle that average wages have to be competitive on the labor market of the financial sector.

Training of employees

In 2008, the Financial Supervision Authority's policy for training and development of its employees was updated in order to better guide the professional self-education to its employees. It is clear that only highly qualified, professional and motivated employees are able to ensure the performance of demanding tasks specified in the Financial Supervision Authority Act. Training planning is based on strategic needs of the organization and personal development needs of each and every employee. These personal development needs are identified by individual eye-to-eye evaluation, assessing also previous working results of an employee and setting new objectives for the next period.

In 2008, employees of the Financial Supervision Authority participated both in national and international training events. Furthermore, also professional in-house training events were organized. Training expenses accounted approximately for 5% of salary expenditures. Training expenses per employee amounted to 17,096 kroons (including travel expenses).

Study visits and secondments in foreign supervisory authorities and in other international organizations are part of employees' training and development concept. Besides exchanging knowledge and experiences, the aim of such activities is to develop a single supervisory culture and to promote collaboration between supervisory authorities.

3.2.4. Summary by the Internal Auditor

The position of the Internal Auditor of the Financial Supervision Authority has been created pursuant to the Financial Supervision Authority Act. The Internal Auditor is subordinated and reports to the Management Board. The Management Board of the Financial Supervision Authority directs the activities of the Internal Auditor by approving the Internal Auditor's strategic plan for four years as well as more detailed working plans for every quarter. The mission of the Internal Auditor is to assist the management in achieving the goals of the organization in the best possible way and at reasonable cost. In planning and performing his activities, the Internal Auditor followed the principles of the IIA (The Institute of Internal Auditors) Code of Ethics. He followed international internal auditing standards to the extent possible and reasonable in a small organization.

The Internal Auditor was able to perform his tasks independently and objectively. In 2008, there were no significant changes in the Internal Auditor's main tasks or his organization of work, and his collaboration with the Management Board was excellent. The Management Board discussed the Internal Auditor's memoranda and audit results in the order of submission, as well as the Internal Auditor's statement of operations and his summary of major risks on a quarterly basis.

The Internal Auditor's activities in internal auditing area were mainly based on his Strategic Plan 2007–2010, based on which the Internal Auditor audited mainly the following two areas in 2008: core activity of the Financial Supervision Authority, i.e. carrying out financial supervision, and the internal life and organization of work within the Authority. The most important areas covered by audits of the Authority's core activity included the evaluation of procedures for handling license applications of credit institutions, major cases for supervision, the process of supervisory risk assessment of the Authority and the advisory guidelines guiding the activities of market participants. The Internal Auditor focused also on evaluating the activities of the Authority in notifying the consumers of financial services, including on evaluating the availability and usability of information presented via consumer education portal. The most important areas covered by audits of the Authority's internal life and organization of work included the evaluation of following issues: the Authority's remuneration and motivation system, mapping of training needs and the arrangement of trainings, implementation of the new operations procedure, the purposefulness and legality of using database charts, the practices of using and granting access to databases, and the process of handling received invoices. The Internal Auditor evaluated also the arrangement of the opinion survey that encompassed supervised entities.

The Internal Auditor discovered no cases of significant misuse or misapplication of funds nor any significant violations of budgetary discipline during the audits of the Authority's internal life and organization of work and the proceedings conducted by the Internal Auditor in 2008. Management and control systems of the Financial Supervision Authority functioned, to a large extent, as might have been reasonably expected. The level of discipline was high when implementing decisions of the Supervisory Board and the Management Board, as well as directives from the Chairman of the Management Board.

The Internal Auditor considers that the Management Board provided continuous support in 2008 for raising the reputation and credibility of the Authority and for improving its competitiveness on the labor market.

The rules for the prevention of conflicts of interests functioned according to the requirements provided by law, and the officials of the Financial Supervision Authority regarded the prevention of conflicts of interests with adequate sense of responsibility. Nevertheless, seven years of experience show that it is in the interests of legal clarity and legal certainty to amend the existing legislation on the prevention and detection of possible conflicts of interests.

3.3. Supervisory activities

3.3.1. Issuing new licenses and registering prospectuses for public offers

Issuing of licenses

In 2008, the Financial Supervision Authority granted authorizations to three new fund management companies and issued a supplementary license to one fund management company already operating on the market. Fund management licenses were granted to AS Limestone Investment Management and AS Redgate Varahaldus (now AS Redgate Asset Management). Nordea Pensions Estonia AS was authorized as a fund management company for managing mandatory and voluntary pension funds. ERGO Varahalduse AS received a supplementary license for managing voluntary pension funds.

Table 1. Licenses issued in 2008

Field of activity	License holder
Fund management company	AS Limestone Investment Management
Fund management company	AS Redgate Asset Management
Fund management company	ERGO Varahalduse AS (supplementary license)
Fund management company	Nordea Pensions Estonia AS

Pursuant to the amendment to Securities Market Act adopted on the basis of the Markets in Financial Instruments Directive (MiFID), only duly authorized financial institutions may provide investment advice in Estonia. Authorizations are granted by the Financial Supervision Authority. Pursuant to the amendment of 19 November 2008, during the transitional period provided by the law the supervised entities have to inform the Authority about investment services provided and, if necessary, apply for supplementary license for the provision of investment advice.

The following supervised entities were authorized for the provision of investment advice using simplified proceedings: AS Avaron Asset Management, AS Danske Capital, AS GILD Financial Advisory Services, AS Kawe Kapital, AS KIT Finance Europe, AS LHV Varahaldus, AS Lõhmus, Haavel ja Viisemann, AS SEB Pank, AS SEB Varahaldus, Swedbank AS (AS Hansapank until 17 March 2009), AS Trigon Alternative Funds, AS Trigon Funds, AS Trigon Securities, Cresco Väärtpaberite AS, Ergo Varahalduse AS, Evli Securities AS, Marfin Pank Eesti AS. AS Gild Fund Management received the license for the provision of investment advice using general proceeding.

Branch licenses (freedom of establishment)

Branches of financial institutions of European Union (EU) Member States operating in Estonia can offer any of the financial services which they are authorized to offer in their home country. The supervision of such financial institutions from other EU Member States is based on the principle of mutual trust. The supervisory agency in the country of origin is responsible for supervising such branches. Branches are not subject to local capital requirements and restrictions.

Despite this, the Financial Supervision Authority still requires supervisory reports to be submitted by branches of foreign credit institutions, in order to examine how the activities of these branches may affect market participants acting on the basis of a license issued in Estonia. Where a foreign financial institution offers its services in Estonia through a subsidiary undertaking, the Financial Supervision Authority exerts full supervision over this subsidiary undertaking.

In 2008, financial institutions registered in other EU Member States established three branches in Estonian:

Table 2. Branches established in Estonia in 2008

Field of activity	Branch in Estonia
Credit institution	Pohjola Bank Plc Estonian Branch
Credit institution	Danske Bank A/S Estonian Branch
Credit institution	AB Bankas Snoras Estonian Branch

Major holding proceedings

Persons who wish to acquire a major holding in a financial institution that is authorized in Estonia must meet the so-called fit&proper criteria. The main requirements are: impeccable business reputation, transparent business relations and the ability to ensure prudent management of the company. If the Financial Supervision Authority considers that the respective person does not meet these criteria, it is entitled to prohibit the acquisition of a major holding.

In 2008, the Financial Supervision Authority conducted 3 major holding proceedings. The Financial Supervision Authority adopted a confirmative decision in all these cases.

Table 3. Major holdings acquired in 2008

Field of activity	Entity	Applicant
Fund management company	AS GILD Property Asset Management	AS GILD Partners
Insurer	Seesam Life Insurance SE	Wiener Städtische Versicherung AG Vienna Insurance Group
Credit institution	Tallinna Äripanga AS	AS Leonarda Invest

Provision of cross-border services

Financial institutions authorized in other EU Member States need not apply to the Financial Supervision Authority for a license to provide financial services in Estonia. The provision of cross-border services may commence after the foreign supervisory agency has informed the Financial Supervision Authority of the financial institution's wish to offer its services in Estonia and has communicated the information required by legislation. In 2008, the growth in the number of providers of cross-border services continued, in particular in the area of investment services.

Table 4. Providers of cross-border services in Estonia

	Number of providers, 31.12.2008	Number of providers, 31.12.2007
Banking services	219	183
Investment services	886	367
Non-life insurance services	313	272
Life insurance services	80	64
Insurance broker services	736	615
Insurance agent services	1170	1082
Fund management services	10	9
Investment funds	62	58
E-money services	13	7

Inclusion into the list of insurance intermediaries

In Estonia, insurance intermediaries include insurance brokers and insurance agents. Insurance brokers represent the interests of policyholders. An insurance agent mediating services of a specific insurer represents the interest of that insurer. As at 31 December 2008, there were 26 insurance brokers and 1003 insurance agents operating in Estonia.

6 new insurance brokers were included into the list of insurance brokers in 2008:

Table 5. Insurance brokers included into the list in 2008

Insurance broker	Clemenc Kindlustusmaakler OÜ
Insurance broker	AAA Kindlustusmaakler OÜ
Insurance broker	Smart Kindlustusmaakler AS
Insurance broker	Fix-Kindlustus Kindlustusmaakler OÜ
Insurance broker	Credo Kindlustusmaaklerid OÜ
Insurance broker	OÜ Kindlustusmaakler Tiina Naur

Insurance agents are included into the list of insurance agents by the insurance company represented by the agent. The list of insurance agents is available on the website of the Financial Supervision Authority (www.fi.ee).

Registration of prospectuses for public offers and takeover bids

Pursuant to the Securities Market Act, in order to admit securities for trading a proper notation prospectus must be registered with the Financial Supervision Authority and published. In 2008, the Financial Supervision Authority registered 4 prospectuses for public offers: prospectuses for the notation of bonds of AS ABC Grupp, Balti Investeeringute Grupi Pank AS and AS SEB Pank as well as a prospectus for the notation of shares of AS Merko Ehitus.

According to the Securities Market Act, the Financial Supervision Authority verifies the conformity of takeover bids with legislation and approves the prospectus and notice of takeover bid. In 2008, the Financial Supervision Authority approved the takeover bid of Carlsberg Estonia Holding OÜ for the acquisition of 100% shares of Saku Õlletehase AS.

Pursuant to the Rural Municipality and City Budgets Act, closed or public issues of debt instruments of rural municipalities and cities must be registered with the Financial Supervision Authority. In 2008, a prospectus for the closed issue of debt instruments of Tartu was registered with the Financial Supervision Authority.

3.3.2. Risk analysis and monitoring the activities of market participants

Banks

In 2008, the risk analysis of credit institutions was based on traditional monthly and quarterly reports. Major risk areas of credit institutions – credit risk, operational risk, liquidity risk, market risk, etc. – are evaluated during such an analysis based both on quantitative and qualitative information. Results of this analysis provide an important input for planning supervisory activities and are regarded as a primary source of information for planning and performing on-site inspections.

In the light of developments in economic environment and on real estate market, the Financial Supervision Authority focused its attention on the compliance by banks to risk management procedures related to mortgage loans and to lending standards. The Financial Supervision Authority monitors the volume of mortgage loans and changes in conditions for granting loans, financing of commercial real estate and development projects, as well as the quality of mortgage loans. The Financial Supervision Authority performed an additional analysis of the quality of private mortgage loans of 4 major banks – Swedbank AS, AS SEB Pank, Danske Bank A/S Estonian Branch and Nordea Bank Finland PLC Estonian Branch, in order to evaluate better the quality of their loan portfolios. An analysis of loans overdue for more than 60 days demonstrated a significant decline in the quality of private mortgage loans in 2008. As at 31 December 2008, the balance of loans overdue for more than 60 days amounted to approximately 2 billion kroons, i.e. 1.9% of the portfolio of private mortgage loans (0.5% in 2007). All major banks experienced a rapid growth in overdue private loans; nevertheless, capital buffers of banks for covering possible losses are strong. The accumulation of problem loans is clearly distinguishable for loans granted in 2006–2007; such problem loans constituted in total about two thirds of all overdue loans. Performance of obligations is problematic for individuals whose loans remain below 600,000 kroons.

Due to developments on global financial markets, the Financial Supervision Authority focused especially on monitoring the liquidity risk. It performed on regular basis the mapping of banks' situation in ensuring the liquidity and drafted estimates on the occurrence of liquidity risk, as well as assessed the procedures and internal regulations related to the management of liquidity risk.

The Financial Supervision Authority focused also on banks' service standards in providing precontractual information. It adopted 2 new advisory guidelines: Requirements to Precontractual Information on Investment Deposit Terms and Conditions and Requirements to Precontractual Information on Housing Loans. The objective of these guidelines was to guide the credit institutions in disclosing adequate and sufficient information to clients before the conclusion of contract, in order to ensure that they make informed investment and borrowing decisions.

Insurance companies

As at 31 December 2008, there were already 6 branches of foreign non-life insurers operating in Estonia. Life insurers authorized by the Financial Supervision Authority had extended their operations into neighboring countries. Thus, the cooperation with supervisory authorities of other countries is becoming continuously more important in the supervision of insurance companies.

As for the supervision of non-life insurers, the Financial Supervision Authority focused mostly on the claims handling procedure and on the application of its Advisory Guidelines on General Requirements to Insurance Contracts. As for the supervision of life insurers, the Authority continued to perform so-called stress or strength tests in order to assess the effects of the financial markets' decline on insurers.

The Financial Supervision Authority performs also quarterly risk-based analysis on developments in the insurance sector. In addition to regular analysis, several special analyses were performed in 2008. E.g. it participated in drafting general principles for mandatory funded pension payments. Persons who have joined the mandatory funded pension scheme and reached to the age when they are entitled (since 1 January 2009) to receive old-age pension, are entitled to receive funded pension payments also through concluding an insurance contract (one option). The Financial Supervision Authority focused also on analyzing various pension payment options as well as principles for the calculation of technical provisions and profit distribution. The Financial Supervision Authority made several *ad hoc* inquiries focusing on insurers in the second half of 2008 in order to assess the effects of global financial crisis on insurers. Its main objective was to control the sustainability of insurers in complying with prudential requirements.

Insurance intermediaries

The supervision of insurance intermediaries was primarily focused on developing professional standards for insurance brokers in respect of the identification of policyholder's insurable interest by the broker and the provision of information for the conclusion of an insurance contract. The Financial Supervision Authority controlled the application of its Advisory Guidelines on Requirements to Insurance Mediation by insurance brokers, in order to identify their prudential and professional competence.

In addition, the Financial Supervision Authority monitored the proper performance of asset separation requirement by all insurance brokers in 2008. Pursuant to the Insurance Activities Act, insurance brokers are required to keep the insurance premiums which are paid by a policyholder and which belong to an insurance undertaking on a separate bank account.

Investment and pension funds

In the supervision of investment funds the Financial Supervision Authority focused on verifying the compliance with investment restrictions set for investment and pension funds; it focused especially on this area due to development on financial markets. Monitoring activities of the Financial Supervision Authority were also focused on the verification of pension funds' investments into less liquid instruments that are more exposed to risks.

On the basis of monthly reports submitted by fund management companies, the conformity of investments with investment restrictions provided in legislation as well as funds' terms and conditions are regularly checked. Investment and pension funds registered in Estonia have made approximately 2800 investments in total.

As before, the Financial Supervision Authority paid special attention to controlling the information disclosed to present and potential clients of investment and pension funds.

In 2008, the Financial Supervision Authority analyzed also legal environment in the area of managing and avoiding conflicts of interests of pension fund management companies. As a result of this analysis, it made its proposals for regulating conflicts of interests and especially for regulating the management and avoidance of conflicts of interests in managing mandatory pension funds. Pursuant to the draft lay submitted to the Ministry of Finance, the Financial Supervision Authority envisages to further strengthen the rules for managing and avoiding conflicts of interests of pension fund management companies.

Amendments to the Act that amends the Funded Pensions Act, the Estonian Central Register of Securities Act, the Investment Funds Act, the Insurance Activities Act, the Guarantee Fund Act and the Income Tax Act came into force on 14 November 2008. These amendments enforced the proposals of the Financial Supervision Authority in respect of the simplification and reduction of the model of pension fund fees.

In 2008, the Financial Supervision Authority registered terms and conditions for 10 new investment funds and 9 pension funds as well as amendments to terms and conditions of 17 investment funds and 13 pension funds. When amending the terms and conditions, the Financial Supervision Authority verified their completeness and clearness as well as their conformity with legislation.

The Financial Supervision Authority performs also quarterly risk-based analyses of developments in fund management companies, evaluating *inter alia* the general situation on funds' market as well as monitoring the profitability of fund management companies and controlling the conformity with prudency requirements.

Investment firms

In performing the risk analysis of investment firms, the Financial Supervision Authority focuses more of its attention and supervisory resources on those supervised entities which are more exposed to risks that may affect their sustainability and the preservation of clients' funds. Evaluation of investment firms' financial risks in based on quarterly supervisory reporting. Additional inquiries are made, if necessary, during meetings organized with the management of an investment firm. Additional monthly risk monitoring is performed for major and more active market participants, in order to discover irregularities in due course.

The Financial Supervision Authority focused in the supervision of investment firms on monitoring the application of MiFID and conformity with capital regulation requirements in 2008. It evaluated the conformity with new requirements provided by MiFID amendments in handling clients, evaluating the suitability and adequacy of services as well as settling of clients' complaints.

Due to drastically deteriorating economic environment, the demand for investment services decreased and several investment firms earned losses. Capitalization level of several investment firms came near to established limits due to earned losses. The Financial Supervision Authority focused therefore on risks that may become aggravated if profits continue to decrease and investment firms continue to earn losses. It evaluated also the possibility to raise additional own funds and establish capital reserves.

In a separate misdemeanor proceeding, the Financial Supervision Authority controlled the disclosure of information by AS SEB Pank to the clients of SEB Likviidsusfond. The Authority discovered violation of legislation and imposed a fine of 300,000 kroons to AS SEB Pank for disclosing incorrect and incomplete information.

Securities market

Price corrections occuring on global securities markets in 2008 had an effect also on securities traded on NASDAQ OMX Tallinn Stock Exchange. Deteriorating economic environment leads generally to increasing pressure on companies' economic indicators, putting to the test the management of companies and its transparency, and to increasing temptation to benefit illegally from securities transactions or avoid losses. The Financial Supervision Authority focused on both of these aspects in the supervision of securities market throughout 2008.

Correct and transparent economic reporting is one of the main bases of investment decisions. Therefore it is essential to ensure the quality, trustworthiness and consistency of input to analysis. In 2008, the Handbook of Financial Reporting Control was prepared together with the relevant risk matrix which was based on the standard of the Committee of European Securities Regulators (CESR) (Standard No. 1 on Financial Information; Enforcement of Standards on Financial Information in Europe, 12.3.2003, CESR/03-073). Pursuant to this Handbook, the Financial Supervision Authority focused on in-depth control of financial reporting by issuers having problems and collaborated closely with both NASDAQ OMX Tallinn Stock Exchange and issuers in order to rectify deficiencies.

In respect of transparency of issuers' management practices, the Financial Supervision Authority performed an analysis of issuers' practices of Good Corporate Governance in December 2007 and August 2008; it discovered that issuers had applied different levels of prudency when preparing reports on Good Corporate Governance Practices presented as a part of annual accounts of 2006 and 2007. Nevertheless, the adoption of Principles of Good Corporate Governance has generally increased the transparency of corporate governance and respective reports have rather been prepared on a good or anticipated level considering that the system was still in its initial phase. Main deficiencies identified were: issuers had not verified their management practices against all proposals of Good Corporate Governance Principles and many reports thus did not reveal the differences between issuer's management practices and Good Corporate Governance Principles. This may mislead shareholders and make them believe that issuers are in conformity with Good Corporate Governance Principles. Secondly, several issuers did not explain the reasons for differences between their management practices and Good Corporate Governance Principles. Third, there were deficiencies in disclosing the required information. Reports frequently include references to other documents or parts of the management report instead of direct disclosure of information, making it more difficult and time-consuming to find the information. The required information is not fully published on issuers' websites and in a couple of cases the issuer's corporate information was available only in English. Several notices for calling a general meeting were incomplete.

The Financial Supervision Authority is planning to open a discussion with issuers and relevant public institutions for drafting regulative requirements in order to rectify these deficiencies mentioned above.

Regular monitoring of trading in securities is performed continuously; in addition, the Authority performs *ad hoc* analyses based on information received from the market. Regular day-to-day monitoring of transactions with shares revealed practices that are not in conformity with generally accepted principles, leading to the opening of misdemeanor proceedings. The Financial Supervision Authority considers it important to improve the cooperation in this area with other public structures, primarily with the police and prosecutor's office.

In addition, the Authority controlled also legal and private persons who had caused suspicion that they may provide investment services without the respective authorization and try to raise funds illegally. The Financial Supervision Authority controlled also reports on transactions of persons specified in Article 188^{13} of the Securities Market Act who are required to disclose and submit to the Supervision Authority trading reports, i.e. the manager of an issuer, persons close to him or her and a legal person associated with the issuer. Five misdemeanor proceedings were initiated.

3.3.3. On-site inspection of market participants

Banks

In 2008, the Financial Supervision Authority conducted on-site inspections in the following credit institutions: AS BIGBANK, AS SEB Pank, Swedbank AS and Tallinna Äripanga AS.

These on-site inspections covered the following areas:

- Credit activities and management of credit risk;
- Reporting on credit activities;
- Performance consistency arrangement;
- Conformity of procedures for the prevention of money laundering and terrorist financing with the provisions of the new Money Laundering and Terrorist Financing Prevention Act and international practices;
- Due diligence measures applied to clients registered in low-tax regions and efficiency of respective control mechanisms;
- Processes for the management of changes to IT and incidents related to IT, as well as adequacy of measures designed for the management of associated risks;
- Conformity with requirements pursuant to MiFID amendments in assessing the suitability and adequacy of services for clients and in settling of complaints;
- Granting and servicing of loans and solvency of borrowers;
- Procedural arrangements for the evaluation of granted loans and conformity with these arrangements;
- Recovery process of overdue loans;
- Actions of Internal Audit;
- Actions of the management and reporting to the management.

Insurance companies

In 2008, on-site inspections were conducted in the following insurance companies: AS If Eesti Kindlustus, ERGO Kindlustuse AS, Seesam Rahvusvaheline Kindlustuse AS and SE Sampo Life Insurance Baltic.

These on-site inspections covered the following areas:

- Operational risk management arrangements;
- Ensuring of performance consistency;
- Organization of IT area;
- Process of concluding insurance contracts;
- Handling of insurance losses;
- Adequacy of outstanding claims provision and correctness of respective calculation principles;
- Internal control environment and the operation of internal audit function.

Insurance companies authorized by the Financial Supervision Authority have actively extended their insurance activities in Latvia and Lithuania since 2007. In 2008, the activities of branches of a life insurer operating as an European company was for the first time controlled in cooperation with supervisory authorities of all three Baltic countries. This joint supervisory action was aimed at evaluating the cross-border functioning of various functions of the company.

Fund management companies and investment firms

In 2008, 4 on-site inspections were conducted by the Financial Supervision Authority in the following 3 investment firms: Evli Securities AS, AS KIT Finance Europe and Lõhmus, Haavel & Viisemann AS.

These on-site inspections covered the following areas:

- Conformity with requirements pursuant to MiFID amendments in assessing the suitability and adequacy of services for clients and in settling of complaints;
- Organization and functioning of Automatic Order Routing (AOR) of securities;
- Conformity with requirements pursuant to money laundering prevention regulations in creating a relationship with a client and internal control procedures applied for the management of involved funds;
- Conformity of internal processes and internal control systems related to the license application procedure with the requirements of the Credit Institutions Act.

3.3.4. Basel II and internal risk assessment methods

At the beginning of 2008, the banking sector experienced the establishment of new principles of Basel II – a more risk-sensitive capital adequacy framework, which is implemented in the European Union by applying the Directives of 2006/48/EC and 2006/49/EC of the European Parliament and of the Council. Basel II is a new and more risk-sensitive prudential norm for banking; it is aimed at ensuring the adequate coverage of accepted risks with capital, in order to safeguard depositors' assets and ensure the stability of monetary system. Besides, Basel II emphasizes the promotion of good practices in risk management, as it is the risk management that plays the most important role in preventing events that may jeopardize the stability of monetary system.

A requirement to calculate an additional capital requirement for covering the operational risk is an important amendment in the application of Basel II. While methods for calculating regulative minimum capital requirements are more sensitive to risks, the capital adequacy framework based on rules can still not fully encompass unique risk profiles of all market participants. Thus, in addition to the conformity with regulative minimum capital requirements (Pillar 1), the application of Basel II principles requires the parallel application of the Internal Capital Adequacy Assessment Process (Pillar 2). Also, Basel II enables the use of statistical internal risk assessment methods in calculating capital requirements, subject to prior approval by the Financial Supervision Authority.

As the implementation of internal risk assessment methods is allowed only when approved by the Financial Supervision Authority, the Authority commenced with examining applications that were submitted by credit institutions in 2008 for switching over to internal assessment systems for credit risk and operational risk. It assessed the conformity of internal risk assessment methods used by banks for measuring credit and operational risks with regulative quantitative and qualitative requirements. Quantitative requirements cover primarily the forecasting capacity and statistical reliability of internal risk assessment methods. Qualitative requirements cover the reliability of IT infrastructure of risk assessment methods, availability of transparent documentation, functioning of adequate internal controls and integration of risk assessment results into day-to-day decision making processes of the bank. The Financial Supervision Authority carried out several on-site inspections with the participation of supervisory authorities from Sweden and other Baltic countries. In 2008, the Financial Supervision Authority issued one permit to use internal risk assessment methods for credit risk and one permit to use internal risk assessment methods for operational risk.

As Basel II is based on principles and provides some interpretation freedom for both supervisory authorities and market participants, the Financial Supervision Authority pays great attention to drafting respective advisory guidelines, in order to increase the transparency of supervisory activities and promote the application of good risk management practices on the marketplace.

3.3.5. Anti-money laundering

Year 2008 can be considered as revolutionary in the area of money laundering and terrorist financing prevention. The new Money Laundering and Terrorist Financing Prevention Act (MLTFPA) came into force on 28 January 2008. This new Act transposed into Estonian legal system the Directives of the European Parliament and of the Council on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing (Third Money Laundering Directive) and on implementing the Third Money Laundering Directive. This Act strengthened legal provisions regulating the establishment of business relationships and increased the opportunities of the Financial Intelligence Unit to stop transactions, including limiting the disposal of assets subject to the transaction for up to 30 days.

Pursuant to these new rules, the service provider has to know its clients' activities more than before, in order to assess the conformity of company's transactions with its operational and risk profile. Also, the service provider is required to identify the origin of funds used in transactions. Information on the company, its owners and beneficial owners as well as transactions must be verifiable from an independent source. Correctness of presented data must be verified on a regular basis throughout the duration of business relationship. This new Act provides several additional due diligence obligations for service providers. Credit and financial institutions must constantly monitor transactions of their clients and identify transactions that deviate from the client's past behavior or that are of extraordinary or suspicious nature. Service providers are required to inform the Financial Intelligence Unit of all suspicious or extraordinary transactions.

Another important event occurred in February when the Select Committee of Experts on the Evaluation of Anti Money Laundering Measures (Moneyval)[1] organized an evaluation visit to Estonia, followed by the adoption of the evaluation report in December in Strasbourg. Moneyval evaluated the efficiency of Estonian legal system, financial supervision and police. The evaluation was based on methodology for evaluating measures adopted for the implementation of FATF's[2] recommendations for the prevention of money laundering and terrorist financing. The same methodology is used by the IMF. Supervisory activities were mostly evaluated as good or very good. Estonia's activities for the prevention of money laundering, including supervisory activities in this area, were rated very high.

Supervisory activities

In 2008, the supervision of the prevention of money laundering and terrorist financing was focused primarily on the control of due diligence measures applied by market participants. The efficiency of the application of amendments related to the enforcement of the new MLTFPA was evaluated in five credit institutions. Also, the establishment of relationships with non-resident clients is constantly monitored.

Thorough on-site inspections were carried out in Swedbank AS, AS SEB Pank and AS KIT Finance Europe, in order to assess the conformity of internal procedures of these financial institutions with applied legislation and international practices as well as the application of due diligence measures in case of clients registered in low-tax regions. An on-site inspection of AS Eesti Krediidipank (Estonian subsidiary of AS Latvian Biznes Banka) was carried through in cooperation with the Latvian Financial and Capital Markets Commission.

1 Moneyval has performed such an evaluation in most Central and East European countries in recent years. FATF and its subsidiary organizations have used this methodology in evaluating several countries, including Russia, China, Japan and Mexico.

2 *Financial Action Task Force*

Results of inspections demonstrated that general awareness of money laundering risks has increased in credit and financial institutions; institutions are aware of changes in the legal environment and internal procedures are generally in line with revised legislation. Pursuant to cooperation agreements, the Financial Supervision Authority informs also other relevant supervisory authorities of the results of on-site inspections.

Representatives of the Financial Supervision Authority participated on a regular basis in the Money Laundering Working Group of the Estonian Banking Association and in the work of the government committee established for the prevention of money laundering and terrorist financing, discussing mostly the issues related to the Moneyval evaluation and the respective report.

3.4. Transparency of financial services and consumer policy

3.4.1. Priorities of the Financial Supervision Authority and measures for educating consumers

One of the tasks of the Financial Supervision Authority is to identify existing risks for consumers and to give them information and support for making the right choice of financial services. A consumer who is acquainted with financial services enters into a contract with higher level of awareness, limiting thus the possibility of subsequent disputes with the financial services provider. The competence of a consumer in concluding a contract adds significant value to ensuring the effective functioning of the market.

In the light of these objectives, the Authority launched and developed further its online portal www.minuraha.ee addressed to consumers. In 2008, significant efforts were made in this area for reaching different social groups. The Financial Supervision Authority launched cooperation projects with the Ministry of Social Affairs for supporting and educating debt advisors and with the Ministry of Education and Research for supplementing national curricula with preparatory training in financial services and products.

Rapid growth in the number of portal users demonstrates that the establishment of consumer portal (www.minuraha.ee) of the Financial Supervision Authority was justified. In 2007 there were 35,869 single visitors and the total number of visits was 46,516. In 2008 the number of single visitors was 81,209 and the total number of visits 117,762. The portal was further developed both in terms of its content and format; news, comments and mocking texts play a more important role in the portal than before. E.g. an interactive consumer game 'Oliver decides!' should intrigue the users to take more interest in financial knowledge. This game is not about checking the existing knowledge but rather about providing new knowledge through practical topics.

The portal was promoted via various channels: special newspapers, fairs, training events, commercials on websites of major daily newspapers, trailers in public transport, printed advertisements, dedicated handouts in major bank and post offices, links on websites of financial services providers, e-mail campaigns, etc.

The cooperation project of the Financial Supervision Authority with the Ministry of Social Affairs for supporting and training debt advisors was based on the need of social workers for additional financial knowledge. In 2008, the Financial Supervision Authority launched a preparation process for developing auxiliary materials for such trainings and received financial support for this process from the Gambling Tax Board. These auxiliary materials will be completed by April 2008.

In 2008, the Authority launched also a cooperation project with the Ministry of Education and Research for supplementing national curricula with preparatory training in financial services and products. It submitted to the National Examination and Qualification Centre its proposals for supplementing the national curriculum of social science with subjects of financial education of consumers; these subjects are included to the program of social science since the academic year 2009/2010. Cooperation will continue in developing new study materials. In cooperation with the Ministry of Education and Research, the Financial Supervision Authority will also organize a national contest on monetary issues addressed to students in 2008, in order to draw their attention to the importance of financial education.

3.4.2. Consumer complaints submitted to the Financial Supervision Authority

The principles and competencies of the Financial Supervision Authority are regulated by the Financial Supervision Authority Act as well as by legislation regulating the conduct of insurance companies, credit institutions, fund management companies and investment firms. The Financial Supervision Authority is not competent to settle complaints by customers of financial services, i.e. to issue mandatory precepts to the parties. It can only provide an independent opinion on a situation at hand and, where necessary, launch supervisory proceedings pursuant to the respective legislation with regard to a bank, an insurance company or any other provider of financial services, in order to ensure the transparency and credibility of financial services market.

On the basis of registration and systematization of complaints, the Financial Supervision Authority gets an overview of main disputes between service providers and consumers on the financial services market and of their frequency.

The number of complaints submitted to the Financial Supervision Authority increased considerably in 2008, especially in the area of banking. The Authority received in total 153 complaints in 2008 (82 complaints in 2007). The number of complaints in the area of banking increased from 24 in 2007 to 95 in 2008. The number of complaints related to travel insurance and voluntary land vehicles insurance has decreased in comparison with 2006. Major share of complaints consisted of complaints submitted against companies belonging to the group of AS SEB Pank (including AS SEB Pank, AS SEB Elu- ja Pensionikindlustus) – in total 70 complaints. 49 complaints were submitted after the revaluation of SEB Likviidsusfond's units by AS SEB Varahaldus. This revaluation did not match clients' expectations because SEB Pank had promoted SEB Likviidsusfond in its sales activities as a totally risk-free investment opportunity.

Number of applications to the Financial Supervision Authority in 2008 by areas of service:

Table 6

Service	No of applications
Investment services	59
Loans/credits	17
Settlements	17
Motor TPL insurance	13
Pension	12
Property insurance	10
Land vehicles insurance	9
Life insurance	4
Deposits	3
Non-life insurance	3
Travel insurance	3
Accident insurance	3
Total	**153**

Number of applications to the Financial Supervision Authority in 2008 by financial institutions:

Table 7

Service provider	No of applications	Market share in its sector[3]
AS SEB Pank	64	21%
Swedbank AS (AS Hansapank until 17 March 2009)	12	49%
If Eesti Kindlustuse AS	11	28%
ERGO Kindlustuse AS	7	22%
Nordea Bank Finland PLC Estonian Branch	8	11%
AS SEB Elu- ja Pensionikindlustus	6	34%
Salva Kindlustuse AS	5	8%
Seesam Rahvusvaheline Kindlustuse AS	5	12%
Danske Bank A/S Estonian Branch	5	12%
Swedbank Elukindlustus AS	4	40%
BTA apdrošināšanas akciju sabiedrība Estonian Branch	4	4%
AS Eesti Krediidipank	3	2%
AAS Gjensidige Baltic Estonian Branch	3	3%
ERGO Elukindlustuse AS	2	6%
AS BIGBANK	2	1%
Swedbank Varakindlustus AS (AS Hansa Varakindlustus until 17 March 2009)	2	14%
Seesam Life Insurance SE	2	8%
AS Inges Kindlustus	2	3%
AS AON Eesti Kindlustusmaakler	1	N/A
Swedbank Investeerimisfondid AS (AS Hansa Investeerimisfondid until 17 March 2009)	1	51%
AS GILD Fund Management	1	7%
Bank DnB NORD A/S Estonian Branch	1	1%
SE Sampo Life Insurance Baltic	1	12%
KindlustusEst Kindlustusmaakler OÜ	1	N/A
Total	**153**	

Application dynamics:

Table 8

	2000	2001	2002	2003	2004	2005	2006	2007	2008
Banks	-	-	26	12	16	28	36	24	95
Insurers	232	86	49	29	41	42	30	56	54
Others	-	-	-	5	1	4	6	2	4
Total	**232**	**86**	**75**	**46**	**58**	**74**	**72**	**82**	**153**

3 Market shares as at 31.12.2008. Market share numbers are rounded; market shares in insurance are based on insurance premium payments, those in banking and fund management are based on the volume of assets. Market shares of life insurers do not include the data of branches.

The majority of complaints submitted to the Financial Supervision Authority in 2008 were related to investment services, loans, settlements, motor TPL insurance, pension saving and property insurance. The share of complaints related to the interpretations of terms and conditions of both investment services contracts and pension insurance contracts has increased.

Other problems related to banking services were primarily caused by different interpretation of terms and conditions of loan agreements or by perfunctory familiarization with parties' rights and obligations by the client before concluding the loan agreement. Problems with settlement services were related to transactions made via cash dispensing machines, everyday settlement transactions and the transparency of bank service fees.

Disputes in the insurance sector were mostly caused by different interpretation of terms and conditions as well as by the fact that customers had a shallow understanding of parties' rights and obligations before entering into an insurance contract. Disputes concerned also adherence to the indemnification deadlines by insurers and their refusal to pay the indemnity.

3.5. Development of regulative environment

Pursuant to Article 6(1)(5) of the Financial Supervision Authority Act, one of the tasks of the Financial Supervision Authority in developing the legal environment is to make proposals for the establishment and amendment of Acts and other legislation concerning the financial sector and related supervision, and participate in the drafting of such Acts and legislation. According to the Financial Supervision Authority Act, draft legislation regulating supervised entities or the activities of the Financial Supervision Authority or having otherwise an effect on the achievement of objectives of financial supervision must be approved by the Financial Supervision Authority.

Introduction

People have a need for security despite the actual economic cycle. Financial sector functions more effectively and takes consumers' interests more into account if the legal framework is clear and stable. Uniform application of legal provisions by the Financial Supervision Authority and adequate speed and objectivity of judicial proceedings is also essential.

As regards the present legal framework, the Financial Supervision Authority recognizes the need for thorough revision of some areas, e.g. conflicts of service providers' interests, uniform regulation of financial services, mechanism for settling extra-judicial disputes caused by financial services. It is also essential to simplify the regulation of certain services (e.g. fund management services). Legislative technique of acts regulating the financial market must also be revised. The Financial Supervision Authority is not directly engaged in legislative activities; still, it has contributed to these activities and is prepared to participate in the development of legislation also in future.

The Authority considers as main deficiencies the lack of mechanism for efficient settlement of extra-judicial disputes and various possibilities to suspend the force of administrative legislation provided by the Financial Supervision Authority.

Consumers may feel themselves powerless in disputes between financial services providers and consumers as ordinary people have to face major financial corporations. Courts have to settle disputes of various natures – from the establishment of paternal filiation to derivative contracts linked to climatic variables. Besides, court actions can be quite time-consuming. Therefore, the Financial Supervision Authority is still of the opinion that it is necessary to follow the example of other European countries and to establish in Estonia a legal framework for settling extra-judicial disputes and a respective body dedicated only to the settlement of disputes arisen in the area of financial services.

The Financial Supervision Authority has came across a case where because of the actions of the opposing party as well as interim legal protection and judicial proceedings, the Authority was entitled to receive necessary requested information from a person only after a year had passed from the adoption of the respective (initial) administrative act. Such a situation is extremely dangerous in crises situations where it is e.g. necessary to subject a bank to extraordinary reporting requirement in order to receive immediately information for assessing the extent of exposure to risk. Delays in receiving such information, not to mention one-year delays, can lead to a situation where the supervisory authority is not aware of the actual situation. This may give rise to a sudden insolvency of a credit institution. It should be mentioned that the suspension of the force of financial supervision authority's administrative acts due to interim legal protection or judicial proceedings is excluded in several EU Member States.

Administrative courts have developed the following fundamental positions in respect of the activities of the Financial Supervision Authority:

- Entities subject to financial supervision have voluntarily subordinated themselves to the supervision by the Financial Supervision Authority, accepting thus the chance that the Authority may supervise them, if necessary;
- The Financial Supervision Authority has a discretionary power to decide the ways of supervision and types of information that have to be gathered for exerting the supervision;
- Requests for information cannot be very detailed due to particularities of the Financial Supervision Authority's work and supervisory activities;
- Statement of objectives in the Financial Supervision Authority's requests for information shall be considered as the performance of clarification and hearing obligation in respect of an addressee;
- Public interest to detect irregularities overrides the interest of an addressee of a request for information to avoid the workload and inconveniences related to requested data.

3.5.1. Overview of the development of regulative environment

In the area of legislative drafting the Financial Supervision Authority would like to emphasize its very good collaboration with the Ministry of Justice and the Ministry of Finance. Main developments occurred in 2008 in the area of legislative drafting (as at 20 February 2009) are described below.

On 28 January 2008 the new **Money Laundering and Terrorist Financing Prevention Act** entered into force, transposing to the Estonian legal system the Directives of the European Parliament and of the Council on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing (Third Money Laundering Directive) and on implementing the Third Money Laundering Directive. A more detailed overview of changes accompanying the new act is available on the website of the Financial Supervision Authority: http://www.fi.ee/?id=2949.

The Regulation No 10 of the Minister of Finance on **Requirements for the Rules of Procedure established by credit and financial institutions and for their implementation and verification of compliance** and the Regulation No 11 of the Minister of Finance on **Criteria of low risk of money laundering and terrorist financing which allows the application of simplified customer due diligence measures** entered into force on 14 April 2008.

On 1 November 2008 **the Advertising Act** entered into force, laying down an obligation of the Financial Supervision Authority to exert supervision over the advertising of financial services that are provided to clients by banks, insurance companies, insurance intermediaries, investment firms, fund management companies, investment and pension funds, participants on the securities market and other entities subject to financial supervision pursuant to Article 2 of the Financial Supervision Authority Act.

Amendments to the Act amending the Funded Pensions Act, the Estonian Central Register of Securities Act, the Investment Funds Act, the Insurance Activities Act, the Guarantee Fund Act and the Income Tax Act entered into force on 14 November 2008. Amendments were based on the need to elaborate and update the system of mandatory funded pension by eliminating deficiencies revealed by analyses and to establish a legal basis for making mandatory funded pension payments. The Ministry of Finance examined the functioning of and developments on pension funds' market together with the Financial Supervision Authority and some of the amendments are based on results of the Authority's analyses.

In **the Law Enforcement Act** it is envisaged to treat the Financial Supervision Authority as a law enforcement authority, adding thereby several new functions. In connection with preparing the Law Enforcement Draft Act, the Financial Supervision Authority made proposals for elaborating the status and competencies of the Authority as a law enforcement authority. The second reading of the Law Enforcement Draft Act in the *Riigikogu* was suspended on 17 December 2008 on the proposal of the Legal Affairs Committee, as it envisages continuing work on preparing the act implementing the Law Enforcement, and the Financial Supervision Authority will also participate in this work.

The Financial Supervision Authority presented also its opinion on **motions to amend the regulation of acquisition and disposal of qualifying holdings in entities subject to financial supervision.** With the draft act that amends the Insurance Activities Act, the Securities Market Act, the Credit Institutions Act, the Investment Funds Act and the Estonian Central Register of Securities Act it is envisaged to harmonize the national legislation with procedures and criteria for evaluating the reliability applied to acquisition and increasing of qualifying holdings in the financial sector. In addition, provisions of the Investment Funds Act will be elaborated in respect of the arrangement for conflicts of pension fund managers' interests and provisions of the Insurance Activities Act on own funds will also be amended.

The Financial Supervision Authority received for approval **the Draft Act amending the Authorized Public Accountants Act** that transposes the Directive 2006/43/EC of the European Parliament and of the Council. This Directive regulates statutory audits of annual accounts and consolidated accounts. The Draft Act provides requirements for sworn auditors and the Association of Sworn Auditors and lays down legal bases for their activities. In addition, the Draft Act provides bases for exerting supervision over public sector internal auditors, sworn auditors, the Association of Sworn Auditors and the Board of Auditors. These provisions are not applied to professional activities and qualification requirements of private sector internal auditors. New provisions include the requirement to set up an audit committee in each company and special provision for ensuring transparency and independence. The Authority has doubts whether the imperative requirement to set up an audit committee should also be applied to credit institutions and insurers.

The Financial Supervision Authority analyzed also **the Conciliation Draft Act** and found it to be a generally suitable framework for a potential body to be established for settling extra-judicial disputes on financial services.

The Financial Supervision Authority was involved in the preparation of **the Emergency Situation Draft Act** by designing the framework for regulating an essential service in the financial system and the liability for supervision. In addition, the Authority presented its opinion on **the Draft Act amending the State Budget Act, the Participation in Legal Persons in Private Law by the State Act and the Riigikogu Rules of Procedure and Internal Rules Act.** The Draft Act allows the state to be faster and more flexible in interfering with the prevention and resolution of financial crisis. The Authority considers it essential in the state of emergency that the state is capable of involving adequate resources from the market and investing them quickly. In cooperation with the Bank of Estonia and the Ministry of Finance, the Authority drafted **the plan for amending the Credit Institutions Act** – motions to amend for extending the competence of the supervisory authority, dividing of credit institutions and expropriation of holdings. Amendments are necessary for ensuring that the state can adequately react in potential situations of financial crisis.

The Financial Supervision Authority contributed also to the regulation of covert investigation in **the Code of Criminal Procedure** in order to enable smooth exertion of financial supervision especially in the area of securities market.

In transposing the Directive 2006/46/EC, the Financial Supervision Authority consulted through **the Act amending the Accounting Act and the Securities Market Act** also the drafting of a legal framework for monitoring the conformity with Good Corporate Governance Principles (based on 'comply or explain' approach) and prescribing other issues related to regulating corporate governance.

3.5.2. Harmonization and optimization of reporting

In 2008, the harmonization of accounting and reporting principles applied to supervisory reports was continued. Harmonization took place on two levels: firstly, international harmonization primarily with accounting and reporting principles applied in the European Union; secondly, harmonization between various sectors of the financial market. In the context of integrated financial markets, this harmonization enables to lower significantly the reporting burden and expenses of both national and international financial groups. Uniform accounting principles and reporting formats facilitate the exchange of information between different supervisory authorities, increasing thus the efficiency of financial supervision.

In 2007 the harmonization was focused on reports of banks; in 2008 the focus was diverted to the reports of investment firms and fund management companies. New reports on prudential norms were established for investment firms in connection with the implementation of Basel II – the new more risk-sensitive capital adequacy framework – in summer 2008. These reports are based on the set of reports developed by CEBS[4] and used for reporting on prudential norms for banks and investment firms in many EU Member States.

New financial reporting formats based on International Financial Reporting Standards (IFRS) were established for investment firms. While the using of IFRS is mandatory for investment firms pursuant to the Accounting Act, this enables the investment firms to submit financial data to different parties on the basis of uniform principles and in the same format. Reporting formats are based on the common set of financial reports developed by CEBS. Investment firms are obliged to use new reporting formats since 2009.

New supervisory financial reporting formats were developed also for fund management companies. Pursuant to the Accounting Act, fund management companies may apply either the accounting principles generally accepted in Estonia or the IFRS for preparing their accounts, and one of the objectives was to introduce reporting formats that would allow submitting data under both the accounting principles generally accepted in Estonia and the IFRS. New financial reporting formats for fund management companies will be taken into use in the first quarter of 2009.

Work on reporting formats for insurers will be continued in 2009.

[4] Committee of European Banking Supervisors

3.5.3. Advisory Guidelines issued by the Financial Supervision Authority

The aim of the advisory guidelines issued by the Financial Supervision Authority is to explain the legislative provisions that apply to activities in the financial sector and to ensure that supervised entities behave in accordance with legislative requirements. Besides explaining legislative provisions and guiding the activities of supervised entities, the advisory guidelines are aimed at reducing regulative competitive advantages and legal risks of market participants in designing their behavior, as well as promoting good practice in the financial sector.

In 2008, the following Advisory Guidelines approved by the Financial Supervision Authority in 2007 entered into force:

Table 9

Guidelines	Enforcement
Requirements to the Internal Capital Adequacy Assessment Process	1 January 2008
General Requirements to Insurance Contracts (amendments)	1 February 2008
General Requirements to Insurance Mediation	1 February 2008

In 2008, the Financial Supervision Authority approved the following Advisory Guidelines:

Table 10

Guidelines	Enforcement
Requirements to Pre-Contractual Information to be Disclosed on Terms and Conditions of Investment Deposits	8 September 2008
Technical Conditions of Notifying the Financial Supervision Authority of Securities Transactions	3 November 2008
List of Minimum Records Investment Firms are Required to Keep	1 January 2009
Requirements to Pre-Contractual Information to be Disclosed on Housing Loans	15 January 2009
Notification of Suspicion of Market Abuse	31 March 2009
Additional Measures for Preventing Money Laundering and Terrorist Financing in Credit and Financial Institutions	1 April 2009

- **Requirements to Pre-Contractual Information to be Disclosed on Terms and Conditions of Investment Deposits**

The objective of the Advisory Guidelines on Requirements to Pre-Contractual Information to be Disclosed on Terms and Conditions of Investment Deposits (entered into force on 8 September 2008) is to instruct persons who receive deposits from the public under investment deposit contracts to disclose adequate and sufficient information on investment deposit's terms and conditions before concluding a contract with the client. The Financial Supervision Authority considers that such disclosure would protect clients' interests when their funds are being used and ensures that informed investment decisions are made.

- **Technical Conditions of Notifying the Financial Supervision Authority of Securities Transactions**

The Advisory Guidelines on Technical Conditions of Notifying the Financial Supervision Authority of Securities Transactions (entered into force on 3 November 2008) are drafted on the basis of Article 2(2) of the Regulation No 52 of the Minister of Finance of 14 July 2007 on the Procedure for Notification of Financial Supervision Authority of Securities Transactions and Articles 12(1)(e) and 13(1) of the Commission Regulation (EC) No 1287/2006. It lays down technical conditions for notification of the Financial Supervision Authority of transaction data on securities admitted for trading on regulated markets.

- **List of Minimum Records Investment Firms are Required to Keep**

The Advisory Guidelines on the List of Minimum Records Investment Firms are Required to Keep (entered into force on 1 January 2009) was adopted on the basis of Article 90(8) of the Securities Market Act. Pursuant to this Article, the Financial Supervision Authority must draw up a list of the records investment firms are required to keep. The list is based on the recommendation of CESR for competent authorities in respect of the list of minimum records investment firms are required to keep under Article 51(3) of the Directive implementing the MiFID.

- **Requirements to Pre-Contractual Information to be Disclosed on Housing Loans**

The Advisory Guidelines on the Requirements to Pre-Contractual Information to be Disclosed on Housing Loans (entered into force on 15 January 2009) were drafted because of the need to instruct credit institutions to disclose adequate and sufficient information on housing loan's terms and conditions before concluding a contract with the client, in order to ensure that informed loan decisions are made. These Advisory Guidelines enhance the transparency of service and help the client to better understand the nature of service, increasing thus the possibility that further potential disputes can be avoided.

- **Notification of Suspicion of Market Abuse**

These Advisory Guidelines cover the obligation of persons who provide investment services to notify the Financial Supervision Authority of reasonable suspicion of market abuse. It also specifies the information the Financial Supervision Authority would like to receive from investment firms in case of suspicion of market abuse and the form of notification. In addition, it lays down the behavior of investment firms in case of suspicion of market abuse and likely signs that refer to the violation of prohibition to make transactions on the basis of inside information. These Advisory Guidelines entered into force on 31 March 2009.

- **Additional Measures for Preventing Money Laundering and Terrorist Financing in Credit and Financial Institutions**

The Advisory Guidelines on Additional Measures for Preventing Money Laundering and Terrorist Financing in Credit and Financial Institutions (adopted on 22 October 2008 by the Decision of the Management Board of the Financial Supervision Authority) provide guiding and explanatory instructions to obligated persons for the application of due diligence measures under the Money Laundering and Terrorist Financing Prevention Act. Annex to the Guidelines provides examples of instruments of constitution for companies registered in low-tax regions, in order to minimize risks associated to the abuse of documents of companies registered in such regions. The Guidelines entered into force on 1 April 2009.

3.6. International cooperation

More than 90% of the Estonian financial sector is captured by subsidiary undertakings or branches of EU financial institutions, i.e. cross-border financial groups operating in Estonia. As Estonia is one of the EU Member States, its financial sector forms a part of the European integrated financial services market. Estonia's financial stability is directly dependant on efficient and operational information exchange with other EU Member States, especially with Nordic countries. Being integrated to the risk assessment process of Nordic financial groups, the Financial Supervision Authority is mapping developments on financial markets together with its colleagues, in order to ensure timely responses to possible problems. Models used by banks to evaluate accepted risks and the amount of capital required to cover such risks are also subject to approval within the framework of such cooperation.

The Financial Supervision Authority is able to influence the shaping of international supervision customs and policies that have an impact on the Estonian financial market by participating in the work of the EU financial sector supervisory committees: the Committee of European Securities Regulators (CESR), the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) and the Committee of European Banking Supervisors (CEBS).

The development of a legal environment that is suitable for the establishment and development of a common financial market in EU, and its implementation model called Lamfalussy framework in 2001 led to a deeper cooperation between supervisory authorities in the European Union with an aim to improve the quality of EU legal provisions regulating the financial sector and of their implementation.

The Lamfalussy Process is a four-level approach. The first level encompasses regulations and directives proposed by the European Commission or adopted in co-decision procedure by the Council of Europe and the European Parliament. These legal instruments provide framework principles and authorize the European Commission to issue implementing documents. Drafts are prepared by respective committees of supervisory authorities (CESR for securities market, CEBS for banking market and CEIOPS for insurance market) who consult also with market participants. Thus, on the third level, the committees of supervisory authorities of EU Member States look after the uniform implementation of European provisions in EU Member States; they are also authorized to issue advisory guidelines and standards. On the fourth level, the European Commission keeps a tab on whether EU Member States have transposed European legislation into their legal systems. If there has been a failure to transpose a European legal instrument into national legal system or if the transposition has been insufficient, the Commission is entitled to institute proceedings against the respective Member State.

3.6.1. International cooperation within the European Union financial supervision committees

In 2008, representatives of the Financial Supervision Authority participated in the work of 37 different committees or working groups. They took part in 30 plenary meetings of committees or meetings of subgroups. The Authority has appointed 26 employees to participate in various working groups.

- **Committee of European Banking Supervisors (CEBS)** continued its work in solving various issues related to the interpretation of the **Capital Requirements Directive** (Directive 2006/49/EC), reporting, harmonization of supervisory practices and group supervision. Also, it dealt with several issues related to effects of the crises. The Financial Supervision Authority took actively part in the work of the following three expert groups (out of 6 cooperation bodies of CEBS): the Expert Group on Financial Information **(EGFI)**, the working group harmonizing the practices of prudential supervision (*Groupe de Contact,* **GdC)** and working groups of Pillar 2 Convergence Network (**P2CN)** engaged in harmonization of supervisory practices under *Groupe de Contact*. Comparative analyses on the implementation of directives on banking supervision have become an important tool for CEBS (similarly to other committees). This objective is pursued by the **Review Panel** of CEBS.

Expert Group on Financial Information **(EGFI)** is a working group focused on the issues of auditing and accounting, and its task is to analyze the influence that the developments taking place in the areas of accounting and auditing have on the banking sector. At the same time, the working group engaged in accounting and auditing issues plays a leading role in harmonizing supervisory reporting. All third-level committees have commenced with developing simplified common information and reporting formats. Consequently, all EU banks, insurance companies and major investment companies should complete and submit to the supervisory authority in future only one consolidated full set of reports. Implementation phase of these new formats will begin in 2010 and the implementation must be completed by 2012.

Groupe de Contact operating under CEBS is focused on the harmonization of prudential supervisory practices and information exchange between national supervisory authorities. Due to the global financial crisis, this working group has been mostly focused on the exchange of supervisory information, evaluation of effects and risks as well as preparation of necessary amendments to regulations since the second part of 2008.The Financial Supervision Authority participates also in the work of two GdC working subgroups. **Pillar 2 Convergence Network** (P2CN*)* in engaged in analyzing and evaluating technical issues related to internal processes and risk management. This issue is of essential importance also for Estonia because different supervisory arrangements may lead to the distortion of competition on the market. The task of **Supervisory Operational Network** (SON) encompassing major banking groups is to support the cooperation network for group supervision as well as to develop best practices in group supervision.

- **The Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS)** continued in 2008 the preparation for implementing the directive on the new capital adequacy framework **Solvency II** both in life and non-life insurance. In the end of 2008, the draft of Solvency II framework directive was submitted to the Council of Europe and the European Parliament. Experts of the Financial Supervision Authority contributed to the work of all four Solvency II expert groups in 2008. The objective of the Financial Supervision Authority is to ensure that also the specialty of Estonia as a small market economy is taken account in this new regulation. An efficient method for developing technical measures necessary for the introduction of the risk-based approach of the directive has been the **Quantitative Impact Study (QIS)** carried out among market participants. The report of the fourth survey (**QIS 4**) ordered by the European Commission was published at the beginning of November 2008. Estonian insurance companies took an active part in this impact study and Estonia had a leading role among EU Member States in terms of participation.

The Financial Requirements Expert Group is dealing with issues related to **standard capital requirements of Solvency II,** e.g. development of standard requirements for technical provisions and capital adequacy both in non-life and life insurance. An important issue in 2008 has been the development of proportionality principles with an aim to identify the adequate criteria for insurance companies. Insurance companies could use simplified methods for calculating provisions and capital requirements if they meet these criteria. Solvency II must be feasibly applicable also to smaller and medium-sized insurers. This principle is important also for Estonian insurance companies.

Internal Governance, Supervisory Review and Reporting Expert Group is mostly dealing with the development of qualitative requirements for the management of insurers as well as the development of uniform supervisory practices. In 2008, the expert group prepared several consultation papers for the European Commission, addressing internal management procedures, risks and solvency requirements. The common reporting format is envisaged to be applied to insurance companies within the framework of Solvency II only since 2012. A common clear concept for insurance reporting will be elaborated (similarly to the banking sector), specifying records to be collected by supervisory authorities and the data to be disclosed in order to ensure the market discipline.

The task of **the Internal Models Expert Group** is to set general and specific requirements under the Solvency II framework for the development of complete and partial internal models for the purpose of calculating solvency requirements. Due to the financial crisis a working paper was prepared examining the functioning of internal models for insurance groups in the crisis situation.

Insurance Groups Supervision Committee is a working group dealing with the supervision of insurance groups and its main aim is to improve the cooperation between home and host supervisors of insurance groups and harmonize supervisory practices. In addition, this Committee plays an important role in coordinating the activities of colleges established for supervising insurance groups. At present, Estonia belongs into three supervisory cooperation councils: Vienna Insurance Group, Sampo plc and If P&C.

Besides Solvency II working groups, the Financial Supervision Authority participates also in the work of **the Committee on Consumer Protection (CCP)** of CEIOPS dealing with **consumer protection** issues.

- **The Committee of European Securities Regulators (CESR)** dealt with issues related to the implementation of five directives in 2008 – **the MiFID** or the Markets in Financial Instruments Directive, **the Transparency Directive**, **the Prospectus Directive**, **the Market Abuse Directive**, and the so-called **UCITS Directive** or the Undertakings for Collective Investment in Transferable Securities Directive. The Financial Supervision Authority participated in the work of ten expert groups of CESR in 2008.

The Financial Supervision Authority was involved in the work of **CESR-POL** expert group and its subgroups, which coordinate the collaboration of CESR members in order to enhance the transparency, efficiency and integration of the European securities market. CESR-POL is also dealing with the effective implementation of the Market Abuse Directive (MAD) 2003/6/EC and the creation of a common market abuse database for EU Member States. In order to harmonize international practices in securities supervision, various cases are being discussed in the expert group **CESR-FIN** and in the working group of **the European Enforcers Coordination Sessions (EECS).** The **Investment Management** expert group of CERS consults the European Commission in preparing a draft act amending the UCITS Directive 85/611/EC (Undertakings for Collective Investment in Transferable Securities Directive) in order to simplify the cross-border offering of funds. In the context of launching the pan-European Transactions Reporting Mechanism (TREM) for securities transactions, established for efficient detection of market abuse, the **CESR-Tech** expert group has prepared the guidelines for the best execution of transaction orders. Expert group of CESR was actively involved in addressing technical issues necessary for the launch of this system. Under the framework of **the Transparency Expert Group** established for drafting implementing provisions of the Transparency Directive 2004/109/EC, also the Officially Appointed Mechanism or the European electronic network based on the MiFID's database is supported.

The Review Panel of CESR is coordinating the performance of comparative analyses in implementing directives related to securities supervision. Following the example of CESR, also other supervisory committees had established such Review Panels.

In addition to sectorial working groups, representatives of the Financial Supervision Authority participate in the work of some cross-sector (so-called 3L3) working groups: the Delegation Task Force **(DTF)** which is dealing with delegation issues and the Anti Money Laundering Task Force **(AMLTF)** which is dealing with the prevention of money laundering. The Delegation Task Force is preparing a recommendation in order to address issues related to the delegation of supervision and liability between home and host countries. Three supervisory committees have also dealt with issues related to the promotion of supervisory convergence as well as organization of exchange and training of personnel of supervisory authorities.

3.6.2. International cooperation within the committees of the system of European central banks

Together with the Bank of Estonia, the Financial Supervision Authority participates in the work of the Banking Supervision Committee **(BSC)** under the auspices of the European Central Bank. Participation in the process of analyzing the EU financial stability and in the information exchange is important for the Financial Supervision Authority's own analyses and for facilitating cooperation in the area of crisis management among supervisory authorities and central banks. The Financial Supervision Authority takes part in the work of two expert groups within the framework of the BCS: the Working Group on Developments in Banking (WGDB) and the Working Group on Macroprudential Analysis (WGMA).

The **WGMA** evaluates the stability of EU financial and banking systems by conducting macroprudential analysis based on aggregate banking data of each EU Member State. In 2008, the expert group dealt mainly with the issues of assessing risks (including liquidity risk) and vulnerability as well as evaluating the effects of secured bonds' market and commercial real estate market on the financial stability. It also focused on evaluating the effects of the global financial crisis on the performance of major banking groups. The objective of the **WGDB** is primarily to analyze and evaluate structural changes in the EU banking sector. In 2008, main discussions concerned the survey performed in the banking sector in 2008 for mapping major risks and the analysis of liquidity management issues of banks.

3.6.3. International cooperation within global organizations

In 2008, the Financial Supervision Authority took indirectly part in the work of such global organizations as the International Association of Insurance Supervisors **(IAIS)**, as well as the BIS Group of Banking Supervisors from Central and Eastern Europe **(BSCEE)** and the International Organization of Securities Commissions **(IOSCO)** established under the Bank of International Settlements. Representatives of the Financial Supervision Authority participated also in annual conferences of these three organizations.

3.6.4. International cooperation on the issues of anti-money laundering and prevention of terrorist financing

In 2008, representatives of the Financial Supervision Authority took an active part in the work of the 3L3 Anti Money Laundering Task Force (AMLTF) of CEBS, CEIOPS and CESR. The Task Force discussed primarily about developing a common understanding on the Regulation (EC) No 1781/2006 of the European Parliament and of the Council on information on the payer accompanying transfers of funds. The main objective of this joint effort was to lay down the criteria which could serve as a basis for the payment intermediary for considering the information inadequate. A compliance person of Swedbank AS was involved in these discussions on the initiative of the Financial Supervision Authority and this person represented credit institutions of Baltic countries in the discussions.

At the end of 2007, a representative of the Financial Supervision Authority was elected to the Moneyval[5] Bureau. The aim of this Bureau is to coordinate the activities of the Committee in preparing and organizing peer reviews in 28 member countries as well as the work of typology working groups.

[5] Moneyval – The Select Committee of Experts on the Evaluation of Anti Money Laundering Measures

3.6.5. Cooperation with foreign supervisory agencies

The Financial Supervision Authority organizes regular meetings and exchanges information with Scandinavian and Baltic financial supervisory agencies. Due to the present market situation, collaboration with the Swedish Financial Supervisory Authority became the priority topic in 2008. The aim of the Financial Supervision Authority in this process of information exchange with the Swedish Financial Supervisory Authority was to get a overview of the effects of developments on global financial markets on parent banks of Estonian credit institutions and to inform the home country supervisor about developments in the Estonian financial sector and risks taken by the entities subject to financial supervision. Year 2008 witnessed also regular multilateral risk meetings between Estonian and Swedish financial supervisors and representatives of parent undertakings of Estonian credit institutions. Negotiations for concluding group-scale agreements of SEB and Swedbank reached to the final phase.

The process of examining applications of credit institutions for switching over to internal evaluation systems for calculating capital requirements of credit and operational risks had commenced already in 2007 and continued also in 2008. Besides the Swedish Financial Supervisory Authority, the Financial Supervision Authority cooperated during this process actively also with Latvian and Lithuanian supervisory authorities.

Several proceedings took place in cooperation with supervisory authorities of other countries. In 2008, the work was continued also in supervisory cooperation colleges. Several meetings between representatives of Scandinavian and Baltic supervisory authorities took place within the framework of these colleges.

In addition to the general cooperation agreement between Estonian and Swedish supervisory authorities, these authorities commenced with preparations in 2008 to conclude a more detailed cooperation agreement covering the principles of exerting supervision over such credit institution groups whose parent undertakings are situated in Sweden.

In the area of insurance supervision, the Financial Supervision Authority considers it essential to collaborate also with Latvian and Lithuanian supervisory authorities, in addition to the cooperation with home country supervisory authorities of insurance companies' branches operating in Estonia. Cooperation with Latvian and Lithuanian supervisory authorities was envisaged primarily in cases where Estonia itself is a home country of an insurance company's branch. The Authority participated in mapping risks of several cross-border insurance groups. E.g. there was a meeting in December 2008 organized in the Finnish supervisory authority where several issues related to OP Pohjola Group, Nordea Bank Finland Group and Evli Bank Group were discussed.

3.6.6. Foreign missions

Cooperation memoranda

On 26 August 2008 the Russian Central Bank (engaged also in the supervision of banking sector) and the Financial Supervision Authority signed the Memorandum of Understanding between the Central Bank of the Russian Federation and the Estonian Financial Supervision Authority, i.e. the cooperation memorandum on banking supervision which had been elaborated for many years. Preparing of the draft of this memorandum started already in spring 2005. The aim of agreeing on cooperation principles was to ensure the stability of banking system in exerting prudential supervision.

In June 2008, the Financial Supervision Authority signed the cooperation memorandum between financial supervisory authorities, central banks and ministries of finance of EU Member States in order to guarantee cross-border financial stability.

In addition, negotiations were started for the preparation of an agreement which would regulate the Nordic cooperation framework for crises management. This is the agreement between central banks, ministries of finance and financial supervisory authorities of Baltic and Nordic countries, within the framework of which also a common crises management framework will be elaborated.

In 2008, the Financial Supervision Authority launched also association negotiations between members of IOSCO[6] in respect of the conclusion of a multilateral cooperation memorandum. Estonia launched also association negotiations with OECD[7] in 2008. The Financial Supervision Authority has an important role to play in receiving an association invitation for Estonia.

In February 2008, the mission of the IMF Financial Sector Assessment Program (FSAP) was organized to Estonia. The aim of this mission was to study the structure of Estonian financial system and the supervisory arrangement as well as to analyze both the situation of Estonian financial sector and the work of the supervisory authority. Prior to the mission, the Authority had to complete several evaluation questionnaires and answer to IMF queries. Meetings focused on such issues as the supervision of securities, insurance and banking, strength or stress tests, reporting, pension insurance and the Financial Supervision Authority as an organization were organized on the initiative of the head of the mission Steven Seelig. The follow-up mission was organized in December 2008 examining the implementation of IMF recommendations. Estonian financial supervision as a whole and especially the work and professionalism of the Authority's employees were ranked very high by the IMF in its report.

The Financial Supervision Authority met with the IMF also in the context of Article IV Mission which performs annual evaluation of financial stability in different countries. Missions to Estonia were organized also by several rating agencies, e.g. Moodys, Fitch and Standard&Poors.

Moneyval's[8] evaluation mission to Estonia took place in February 2008. Estonia's actions to prevent money laundering were ranked very high by the conformity assessment in the Moneyval report. This is a mark of recognition to anti money laundering and terrorist financing measures applied in Estonia as a whole and *inter alia* to supervisory activities in this area.

[6] International Organization of Securities Commissions

[7] Organisation for Economic Cooperation and Development

[8] The Select Committee of Experts on the Evaluation of Anti Money Laundering Measures

4. Financial Supervision Authority's 2008 Annual Report of Revenues and Expenditures

Accounting principles

General remark

The annual report of revenues and expenses has been compiled according to the Financial Supervision Authority Act and applied accounting principles. According to the Bank of Estonia Act, the Financial Supervision Authority does not pay income tax or other taxes related to business activities, except for taxes related to natural persons. Based on § 21 of the Value Added Tax Act, the Financial Supervision Authority is registered as a taxable person with limited liability and calculates VAT on the turnover of goods and services imported or acquired within the European Community. Revenues and expenses of the Financial Supervision Authority are recorded during the accounting period on an accrual basis, regardless of the date when the cash was received or paid. Financial transactions are recorded according to their acquisition cost and at the moment of their completion. The report on revenues and expenses is compiled in thousands of kroons, unless another currency is specified.

Transactions in foreign currency

Foreign currency includes all other currencies other than Estonian kroons (i.e. accounting currency). Reporting of any foreign currency transaction is based on the official exchange rate of the Bank of Estonia on the day of the transaction.

Operating lease

Operating lease is based on a leasing contract where all material risks and benefits related to the property are not conveyed to the lessee. Operating lease is reported straight-line during the leasing period on the Revenue and Expenditure Account as an expense.

Revenue and expenditure account (in thousands of kroons)

	ANNEX	2008	2007
REVENUE			
Supervisory fees	1	58,587	46,184
Other revenue	2	1,991	510
Total operational revenue		**60,578**	**46,694**
EXPENDITURE			
Personnel expenditure	3	37,154	29,036
Misc. operational expenditure	4	19,905	16,854
Other expenditure	5	649	773
Total operational expenditure		**57,708**	**46,663**
Profit for core activities		**2,870**	**31**
Financial income and expenditure	6	4,790	3, 029
Profit for the accounting year		**7,660**	3,060

ANNEXES TO THE ANNUAL REPORT OF REVENUES AND EXPENDITURES

ANNEX 1

Supervisory fee (in thousands of kroons)

	Paid supervisory fees **2008**	Share %	Paid supervisory fees **2007**	Share %
Credit institutions	38,272	65.3%	29,828	64.6%
Non-life insurers	7,026	12.0%	5,500	11.9%
Fund management companies	5,422	9.3%	4,793	10.4%
Life insurers	4,130	7.0%	2,642	5.7%
Investment firms	1,884	3.2%	1,902	4.1%
Insurance brokers	1,853	3.2%	1,519	3.3%
Total	**58,587**	**100%**	**46,184**	**100%**

The financing principles of the Financial Supervision Authority are provided in the Financial Supervision Authority Act. Supervisory fees consist of two components: firstly, the capital component, which is the amount that equals one percent of the total of the minimum (net) own funds, equity or share capital of the supervised entity; secondly, the volume component, which is the amount that equals the percentage of the supervised entity's assets, total amount of insurance payments, calculated assets or commission fees established by the Minister of Finance at the proposal of the Supervisory Board of the Financial Supervision Authority.

When establishing the rates for the volume component of the supervisory fees for different groups of supervised entities, the Authority considers the volume and profitability of their activities, evaluates the resources spent on their supervision, and the final decision is based on the assumption that the supervisory fee should not be excessively burdensome for the entity.

Pre-payments of the capital and volume components of the supervisory fee are made to the Financial Supervision Authority by 31 December of the year preceding the financial year. The final payment of the volume part is made by 30 September.

Supervised entities entering the market during the financial year must pay only the capital component of the supervisory fee in 30 days of acquiring the right to operate.

ANNEX 2

Other revenue (in thousands of kroons)

	2008	2007
Processing fees	485	458
Other revenue	1,506	52
Total	**1,991**	**510**

According to the amendments to the Financial Supervision Authority Act, any natural person, legal person or branch of a foreign company that applies to the Financial Supervision Authority to have an application reviewed or an operation completed pays a processing fee to the Financial Supervision Authority.

The item *Other revenues* shows the cost of fixed-term employment contracts of the Authority's employee for working in CEBS compensated by CEBS.

ANNEX 3

Personnel expenditure (in thousands of kroons)

	2008	2007
Salaries	27,484	21,433
Taxes	9,148	7,171
Supervisory Board compensations	522	432
Total	**37,154**	**29,036**

Salary expenditures primarily include salary expenditures together with bonuses, compensations for members of the Management Board and the increase in the estimated vacation liability for the unused vacation of Financial Supervision Authority employees, including social taxes.

At the end of 2008, the average salary of a specialist of the Financial Supervision Authority amounted to 25,857 kroons per month (23,556 kroons in 2007). In 2008, the total sum of compensation to the Supervisory Board and Management Board members amounted to 4,678 thousand kroons. Total bonuses paid to employees accounted for 11.95% of salary expenditures.

ANNEX 4

Misc. operational expenditure (in thousands of kroons)

	2008	2007
Real estate lease	6,466	4,466
IT systems and development	3,401	2,233
Business trips	3,043	2,471
Office expenses	1,411	2,639
Training expenses	1,128	1,387
Membership fees	1,699	1,465
Accounting expenses	780	780
Lease for fixed assets	214	401
Consumer information, advertising	1,193	418
News agencies	275	168
Personnel search	128	237
Legal assistance and consultation	63	95
Auditing expenses	104	94
Total	**19,905**	**16,854**

Operational expenditure

The item *Real estate lease* includes the office space leased from The Bank of Estonia with a total area of 1399 m² at a price of 266 kroons per m² each month, which includes all costs related to the administration of the office space. It includes also the renovation cost of the office building of the Financial Supervision Authority.

The item *IT systems and development* includes IT services bought from The Bank of Estonia at an estimated value of 30,000 kroons per user and the cost of IT development projects of the Financial Supervision Authority.

The item *Business trips* includes all trips related to representing the Financial Supervision Authority and supervisory cooperation. The item *Business trips* includes all trips related to representing the Financial Supervision Authority and supervisory cooperation. Business trips were primarily related to CESR, CEIOPS and CEBS committee and sub-committee meetings and the development of cooperation with supervisory agencies of the European Union and third countries. Business trip expenses also include the expenses related to the supervision of foreign subsidiaries of supervised entities registered in Estonia. In total, there were 223 business trips in 2008 (192 in 2007).

The item *Office expenses* includes expenses for periodicals and books, translation, office supplies, meetings and representation, phone and transport.

The item *Training expenses* includes the expenses for training locally and abroad, including travel expenses. In 2008, the average cost for training abroad was 19,857 kroons and for local training 4776 kroons. Training was mostly provided in the development of capital regulation in the banking and insurance sectors, supervision of the securities market and development of legal competence. Language training for employees has also been substantially encouraged.

The item *Membership fees* reflects the annual fees for membership in CESR, IAIS, BSCEE, CEIOPS, CEBS and IOSCO.

The item *Accounting expenses* includes cost accounting, partial management accounting, payroll accounting, loan accounting, performance of payments and settlements, purchased from the Bank of Estonia.

The item *Lease for fixed assets* includes the lease paid by the Financial Supervision Authority to the Bank of Estonia. The lease for fixed assets used by the Financial Supervision Authority, including IT hardware and software as well as inventory, is paid per year. The amount of the lease is equal to the depreciation rate at the Bank of Estonia for the specific fixed assets. Tangible fixed assets include assets that are used by the company for its own business activities and which useful life are over 1 year and the cost is over 50 thousand kroons.

The item *Consumer information and advertising* includes the expenses for development and the launch of the Financial Supervision Authority consumer website www.minuraha.ee, the publication of information materials addressed to consumers, and costs associated with the Financial Supervision Authority Yearbook.

Expenses for *news agencies* include user fees for news agencies and the cost of the Financial Supervision Authority website.

The item *Personnel search* includes recruitment costs for the employees of the Financial Supervision Authority.

The item *Legal assistance and consultation* shows expenditures incurred due to the involvement of experts, special audits, legal opinions and legal assistance related to the supervisory activities of the Financial Supervision Authority.

The item *Auditing expenses* includes the expenses of auditing the Report on Revenues and Expenses of the Financial Supervision Authority; according to Article 51(3) of the Financial Supervision Authority Act, the report is audited by an auditor from The Bank of Estonia.

ANNEX 5

Other expenditure (in thousands of kroons)

	2008	2007
Compensation and benefits	326	389
Cultural events and sports	323	384
Total	**649**	**773**

The item *Compensation and benefits* includes maternity support, special support, expenses involved in guaranteeing the health care of employees and expenses related to sporting activities. This item also reflects the compensation of 1/3 of the contributory pension payments to the employees of the Financial Supervision Authority, but not more than 10% of the gross annual salary of an employee.

The item *Culture and sports* reflects the expenditures for events organized for the employees of the Financial Supervision Authority.

ANNEX 6

The Bank of Estonia pays interests based on the average balance of the Financial Supervision Authority's bank account, and the interest rate equals The Bank of Estonia's rate of return on foreign exchange reserves for the previous quarter.

BALANCE SHEET (in thousands of kroons)

ASSETS	**31.12.2008**	**31.12.2007**
Cash and bank accounts	95,939	92,098
Supervisory fees receivables	4,613	1,519
Total assets	**100,552**	**93,617**
LIABILITIES AND RESERVE		
Payables to employees	4,020	3,027
Tax arrears	1,360	1,146
Misc. payables	2,288	7,870
Deferred income	57,495	53,844
Total liabilities	**65,163**	**65,887**
Reserve	27,729	24,670
Profit for the accounting year	7,660	3,060
Total reserve and profit for the accounting year	**35,389**	**27,730**
Total liabilities, reserve and profit for the accounting year	**100,552**	**93,617**

EXPLANATORY NOTES FOR THE 2008 BALANCE SHEET

The item *Cash and bank accounts* shows the balance of current accounts in the Bank of Estonia.

The item *Supervisory fees receivable* shows prepayments of supervisory fees for 2009 not yet received by the Financial Supervision Authority in the amount of 4,613 thousand kroons.

The item *Payables to employees* includes unpaid wages and vacation liabilities.
Unpaid wages not yet paid to the employees of the Financial Supervision Authority amount to 2,394 thousand kroons. Vacation liabilities include the estimated vacation liability for vacation not taken by Financial Supervision Authority employees in the amount of 1,626 thousand kroons.

The item *Tax arrears* shows the tax liability of the Financial Supervision Authority for salaries.

The item *Other payables* includes expenditures by the Financial Supervision Authority covered by the Bank of Estonia in 2008, which the Financial Supervision Authority will compensate to the Bank of Estonia in 2009. The expenses of the Financial Supervision Authority are recorded in the annual report according to the accrual method.

The item *Deferred income* includes the prepayments of 2009 supervisory fees.

Reserve – pursuant to the Resolution of March 2008 of the Supervisory Board of the Financial Supervision Authority it was decided that the 2007 net gain totaling 3,060 thousand kroons will be transferred to the reserve. The reserve totaled 27,729 thousand kroons by year 2008.

The profit for the accounting year 2008 was 7,660 thousand kroons.

5. Independent Auditor's Report

To the Supervisory Board of the Financial Supervision Authority

We have audited the Annual Report of Revenues and Expenditures of the Financial Supervision Authority, consisting of the revenue and expenditure account of the accounting year that ended on 31 December 2008, relevant accounting principles and other explanatory notes.

Responsibility of the Management Board for the Annual Report of Revenues and Expenditures

The Management Board is responsible for the compilation and true and fair presentation of the Annual Report of Revenues and Expenditures, in accordance with the Financial Supervision Authority Act and the accounting principles described in the attached Annual Report of Revenues and Expenditures. Among other things, it is responsible for the development and administration of the relevant internal control system that guarantees the accurate compilation and presentation of the Annual Report of Revenues and Expenditures without material errors caused by fraud or error; for choosing and implementing appropriate accounting principles; and for making accounting assessments that are justified in the given situation.

Liability of the Auditor

Our assignment is to provide an assessment of the Annual Report of Revenues and Expenditures based on the results of our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we follow the rules of ethics, and plan and perform the audit to obtain reasonable assurance that the Annual Report of Revenues and Expenditures is free of material errors.

Our audit includes carrying out procedures to gather evidence about the figures presented and the information disclosed in the Annual Report of Revenues and Expenditures. The auditing procedures depend on the Auditor's assessments, including the assessment of the risk that the Annual Report of Revenues and Expenditures might include material errors caused by fraud or error. In evaluating this risk, the Auditor, with a view to plan appropriate auditing procedures, takes into consideration the internal control system that has been adopted for compiling and presenting the true and fair Annual Report of Revenues and Expenditures, but does not give an assessment of the operation of the system. The audit also includes an assessment of the appropriateness of the accounting principles, of the reasonableness of the accounting assessments of the Management Board and of the general way of presenting the Annual Report of Revenues and Expenditures.

We believe that the audit evidence gathered is sufficient and appropriate for presenting our opinion.

Opinion

In our opinion, the Annual Report of Revenues and Expenditures presents fairly, in all material respects, the financial performance of the Financial Supervision Authority in the accounting year that ended on 31 December 2008, in accordance with the Financial Supervision Authority Act and the accounting principles described in the attached Annual Report of Revenues and Expenditures.

Tiit Raimla
AS PricewaterhouseCoopers
14. märts 2008

Stan Nahkor
Certified auditor

6. Overview of the Estonian Financial Market

6.1. Economic environment

Year 2008 witnessed a significant setback in the global economic environment and the uncertainty over the future continues. Also the economies of Estonia's main trading partners are weakening, putting additional pressure on our economic prospects.

Estonia's economic expansion turned into recession in 2008: the total decline in GDP was 3.6%. While the first quarter of the year still witnessed an expansion of 0.2%, the decline experienced in the second, third and fourth quarter was -1.1%, -3.5% and -9.7%, respectively. Economic downturn was mostly driven by the drop in domestic demand, caused by the deterioration of business conjuncture in main economic sectors as well as by decrease in consumers' sense of security. First months of 2009 have not shown any increase in both operators' and consumers' sense of security. Due to a decrease in external demand also the export of goods and services declined in 2008. Import of goods and services decreased by 7.9%, export by 1.1%. Import has decreased more than export due to the decline in consumption and investments, implicating the improvement of trade balance and reducing current account deficit.

According to the estimates of the Bank of Estonia, Estonia's economic decline may reach up to 12.3% in 2009 due to the drop in external demand. Economic growth is expected to recover in 2010.

The inflation rate increased in 2008 at a much faster pace than in the previous year: average growth in consumer prices was 10.4% (6.6% in 2007). Growth in consumer prices was mostly driven by increasing housing expenses and higher prices of food, fuel, alcoholic beverages and tobacco products. First months of 2009 have witnessed a significant drop in the pace of inflation and the Bank of Estonia estimates that the inflation rate is likely to remain below 2% in 2009.

Unemployment rate that had remained on a low level in the first half of 2008 increased considerably in the second half and reached its highest level in three years by the end of the year. Unemployment rate reached 5.5% in 2008 (4.7% in 2007). Average annual employment actually even increased as compared with 2007. Still, the number of employed people dropped significantly in the last quarter – by 8000 persons in total. Year 2009 is expected to witness continuing growth in the unemployment rate and decreasing employment.

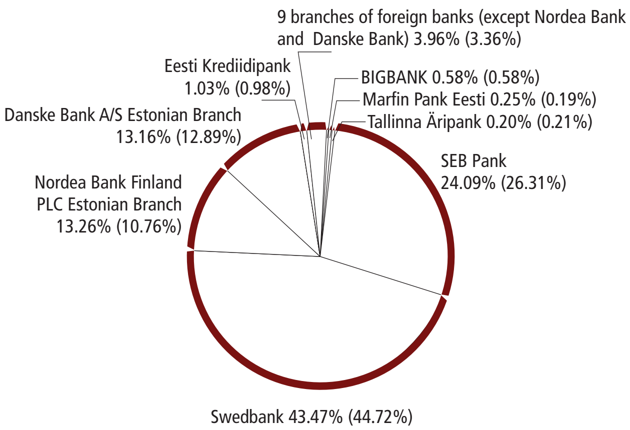
6.2. Credit institutions

As at 31 December 2008, there were six locally authorized credit institutions and ten branches of foreign credit institution operating in Estonia. In 2008, three new market participants were registered: Estonian branches of AB Bankas Snoras, Pohjola Bank plc and Danske Bank A/S Estonian Branch.

Foreign credit institutions' branches are increasing their market share in loans

Competition of banks on the credit market was still very intense in 2008. Estonian branches of Nordea Bank Finland PLC and Danske Bank A/S as well as the Estonian branch of Bank DnB NORD A/S increased their market shares on the credit market[9]. They increased their market shares on the account of major banks – Swedbank AS and AS SEB Pank *(See Figure 1)*. At the end of 2008, the share of these two major banks totaled 68% of the credit market and their market share had decreased by 3% in comparison with the previous year. Lending policy of major banks has become more conservative, in particular when financing the real estate sector. Year 2009 is expected to witness continuing expansion and growth of branches of foreign banks in grabbing the market share.

Figure 1. Market shares of banks based on loans issued to the non-financial sector as at 31.12.2008, in brackets 31.12.2007



9 branches of foreign banks include Bank DnB NORD A/S Estonian Branch, AS Parex banka Estonian Branch, Scania Finans AB Estonian Branch, Siemens Financial Services AB Estonian Branch, Svenska Handelsbanken AB Estonian Branch, AS UniCredit Bank Estonian Branch, Allied Irish Banks, p.l.c. Estonian Branch, AB Bankas Snoras Estonian Branch and Pohjola Bank plc Estonian Branch

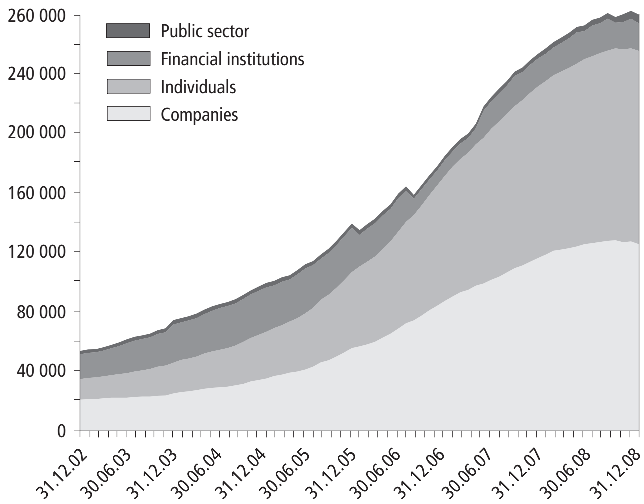
[9] This does not include loans to credit institutions and other financial institutions.

Considerable slowdown in credit growth

Total assets of banks increased by 7% in 2008 and totaled 341.5 billion kroons as at 31 December 2008. Asset volume increase was mostly driven by the 9% growth in clients' loan portfolio (35% in 2007). The combined loan portfolio of banks amounted to 260.4 billion kroons at the end of 2008, forming 76% of total assets.

As at 31 December 2008, the combined loan portfolio of banks was structured as following: loans to companies 45%, loans to individuals 46%, loans to financial institutions 7% and loans to the public sector 2% *(See Figure 2)*. In 2008, loans to companies totalled 116.8 billion kroons and loans to individuals 120.9 billion kroons. Loans to financial institutions amounted to 17.3 billion kroons and loans to the public sector 5.4 billion kroons.

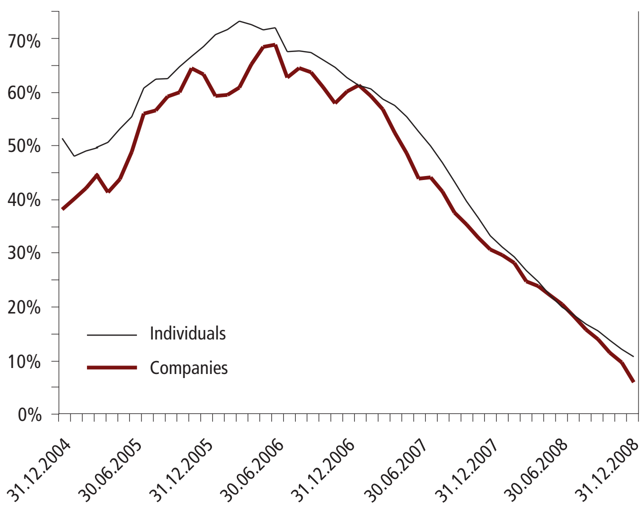
Figure 2. Loan portfolio structure of banks by main customer groups (in millions of kroons)



In 2008, the growth in financing both individuals and companies continued to slow down. While loans to individuals increased 63% in 2006 and 33% in 2007, the growth in financing individuals slowed down to 11% by the end of 2008 *(See Figure 3)*. This is also true for the growth in financing companies, which was 60% in 2006, 31% in 2007, and which slowed down to 6% by the end of 2008. The growth slowed down mostly due to major banks – Swedbank AS and AS SEB Pank.

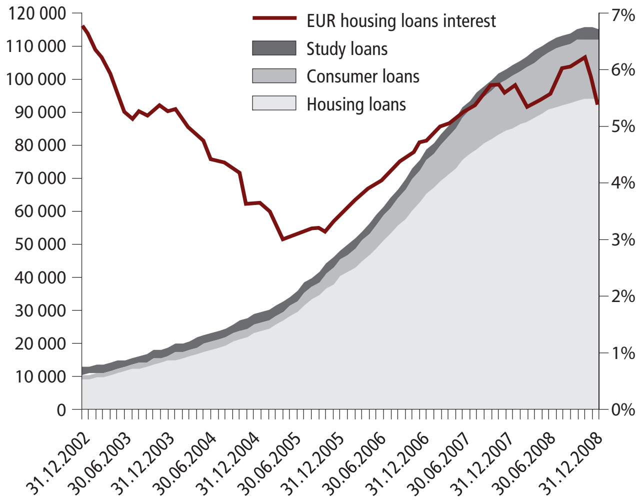
Nevertheless, the loan portfolio of branches of foreign banks kept growing in a fast pace, the growth being 35% in Nordea Bank Finland PLC Estonian Branch, 12% in Danske Bank A/S Estonian Branch, 60% in Bank DnB NORD A/S Estonian Branch and 33% in Svenska Handelsbanken AB Estonian Branch. Slowdown in the growth of loans to individuals is increasingly driven by the decrease in customers' sense of security. Slowdown in the growth of loans to corporate clients is mostly driven by the slowdown in financing the real estate sector. Based on the global and national economic decline, the slowdown in the growth of loan portfolio is expected to continue also in future.

Figure 3. Annual growth in loans to individuals and companies (%)



The growth in both housing and consumer loans slowed down in 2008. As in previous years, the volume of loans to individuals increased in particular due to the growth in housing loans *(See Figure 4)*, which nevertheless experienced a significant slowdown in comparison with previous years. While the growth in housing loans volume was 63% in 2006 and 31% in 2007, it slowed down to 10% by the end of 2008. Slowdown was caused by the decrease in consumers' sense of security affecting their borrowing behavior and the conservative lending policy of banks. Most housing loans are linked to the Euro Interbank Offering Rate (Euribor). In the end of 2008, the decrease in the Euribor led also to a decrease in the average interest rate applied to housing loans: the average interest rate applied to Euro-denominated housing loans had decreased to 5.34% by the end of 2008 (5.76% at the end of 2007).

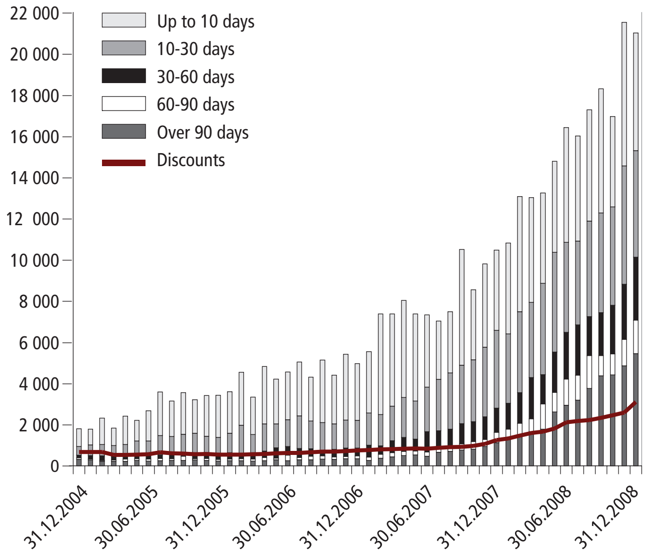
Figure 4. Loans to individuals (in millions of kroons) and Euro-denominated housing loans' interest rate (rhs)



Deteriorating quality of loan portfolio

The quality of banks' loan portfolio deteriorated significantly in 2008. Due to the economic decline, the volume of overdue loans has started to grow, both in absolute terms and as a share of the whole loan portfolio *(See Figure 5)*. The growth was especially strong in loans overdue for more than 90 days in 2008. The percentage of overdue loans formed 0.5% of banks' loan portfolio at the end of 2007, but by the end of 2008 this percentage had reached to 2.1%. Also, the coverage of long-term loans overdue with provisions has declined. Although banks made many new provisions during the years, the volume of overdue loans increased in a much faster pace. While the coverage of loans overdue for more than 90 days was 103% at the beginning of 2008, it had declined to 57% by the end of December. 83% of banks' combined loan portfolio was classified as non-problem[10] loans. Loans classified as doubtful, risky or unlikely formed in total 6% of the composite loan portfolio (3% in 2007). Based on recent developments in the economic environment, the growth of overdue loans and provisions is expected to continue also in 2009.

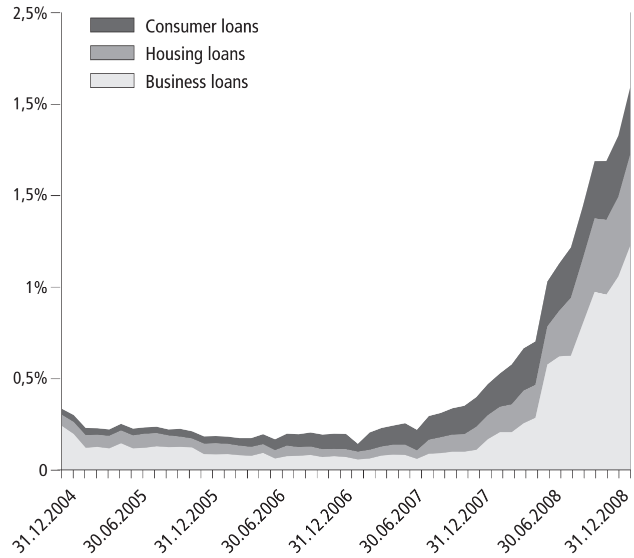
Figure 5. Loans overdue and provisions of banks (in millions of kroons)



10 Classification is based on the Decree No 9 of the Governor of the Bank of Estonia, 27 June 2000.

Loans overdue for more than 90 days increased in 2008 in all product groups: overdue loans included housing loans and consumer loans given to individuals as well as loans given to corporate clients. The growth in loan volume was the biggest and the fastest for business loans overdue *(See Figure 6)*. Loans overdue in the corporate clients' group have increased almost eight times in comparison with the beginning of 2008. Loans overdue in the product group of housing and consumer loans have increased four and two times, respectively. As far as corporate clients are concerned, the growth of loans overdue for more than 90 days was caused mainly by a significant growth of loans overdue related to the real estate sector.

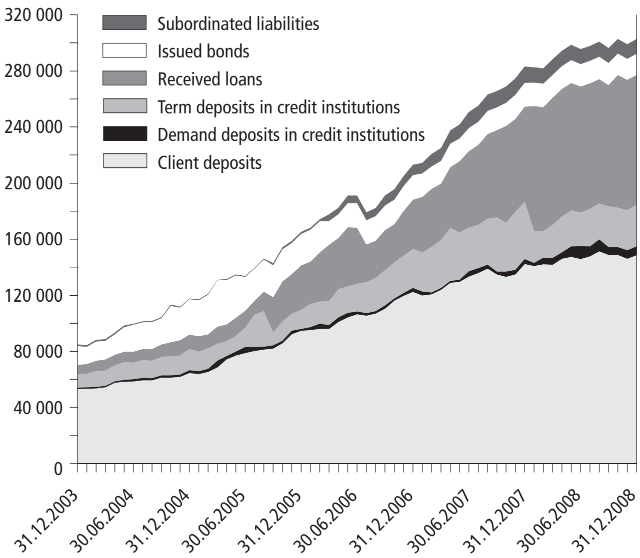
Figure 6. Structure of loans overdue for more than 90 days



Increase mainly in funds received from parent banks

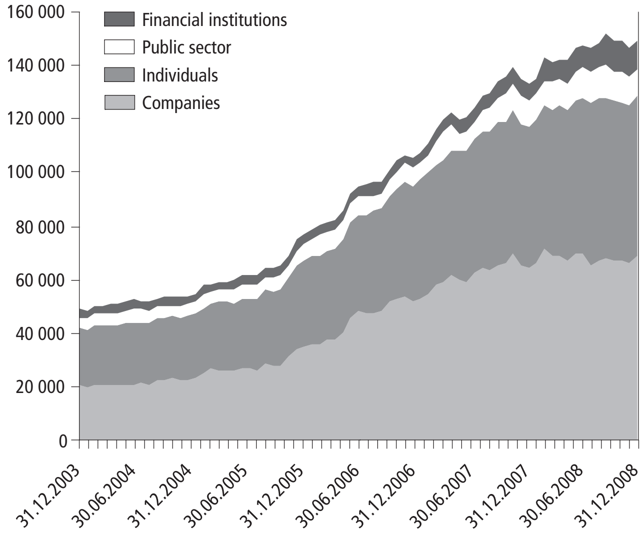
By the end of 2008, the total volume of resources in the banking sector had reached 303 billion kroons, growing by 7% in 2008. By the type of resources, the most substantial increase was in the funds from parent banks, mainly obtained in the form of loans *(See Figure 7)*. Therefore also the share of external institutional borrowing increased: while these loans accounted for 46% of total resources in 2007, their share had increased to 48% by the end of 2008. Clients' deposits formed 48% of total resources of the banking sector at the end of 2008. The share of client deposits has decreased as the financing by parent banks has increased. Local resources deficit is also evident from the loan-deposit ratio that increased by the year-end, reaching the level of 175% (168% in 2007). As the liquidity risk of banks operating in Estonia is generally managed at the level of parent bank groups, the occurrence of risk is directly depending on the ability of the parent bank to refinance its liabilities on money markets and to involve additional funds.

Figure 7. Resources in the banking sector (in millions of kroons)



Client deposits in banks reached almost 149 billion kroons at the end of 2008, the annual growth being 4%. Deposits of companies accounted for the biggest share of deposits, amounting to 68.8 billion kroons or 46% of deposits *(See Figure 8)*. 40% of deposits belonged to individuals, amounting to 59.6 billion kroons. Deposits of the public sector totaled 9.9 billion kroons, forming 7% of all deposits. The share of deposits of financial institutions was approximately the same, totaling 10.6 billion kroons.

Figure 8. Structure of deposits in banks by main client groups (in millions of kroons)

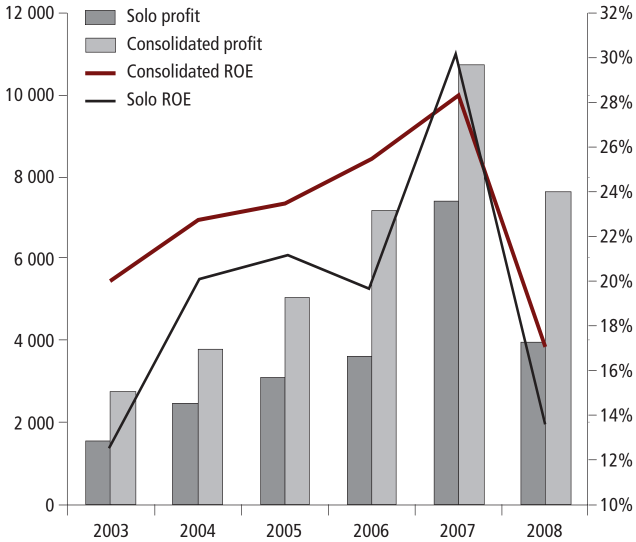


Banks' profitability is decreasing

In 2008, banks operating in Estonia earned on solo basis a net profit of 3.9 billion kroons, which is approximately twice as small as in 2007 *(See Figure 9)*. Still, we have to remember that profits earned in 2007 include extraordinary income of Swedbank AS (AS Hansapank) received as dividends from subsidiary undertakings. Without this extraordinary income, the 2008 profit of banks was only 19% smaller than the profit in 2007. Profits decreased primarily due to significantly higher loan loss provisions: annual increase in loan loss provisions was about fourfold. Banking groups' net profit amounted to 7.6 billion kroons, which was 29% less than in 2007.

Due to the decrease in net profits, also the composite Return on Equity (ROE) has considerably decreased both on solo and consolidated basis: solo ROE was 13.5% and consolidated ROE 17% (30% and 28.3% respectively in 2007). Based on prospects of global and national economy, the profitability of banks is expected to decrease also in future.

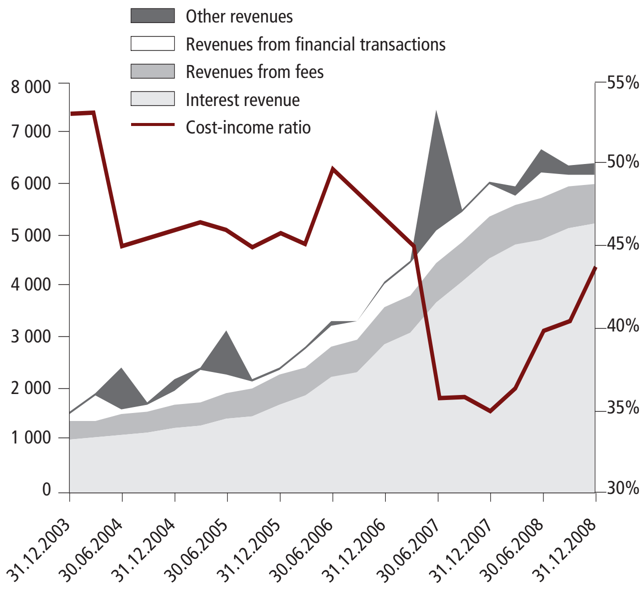
Figure 9. Profits of banks (in millions of kroons) and ROE (rhs)



As was the case in the previous year, banks received revenues in 2008 primarily from traditional banking activities, i.e. from lending. At the end of 2008, interest revenues constituted 79% of the total revenue (66% in 2007). The share has increased during the year, primarily due to small revenues from financial activities and other activities *(See Figure 10).*

Nevertheless, the growth in interest revenues is slowing down and banks' interest costs related to term deposits and funds received from parent banks experiences faster growth than interest revenues. A significant drop in the base rate will also have some downward effect on interest revenues in the nearest future because most of the loans granted in Estonia are linked to the Euribor. Developments on financial markets have lead to considerably shrink revenues from financial transactions: these revenues have decreased almost twice during the year. Decreased revenues have caused an increase in the banks' aggregate cost-benefit ratio to 44% by the end of 2008 (35% in 2007).

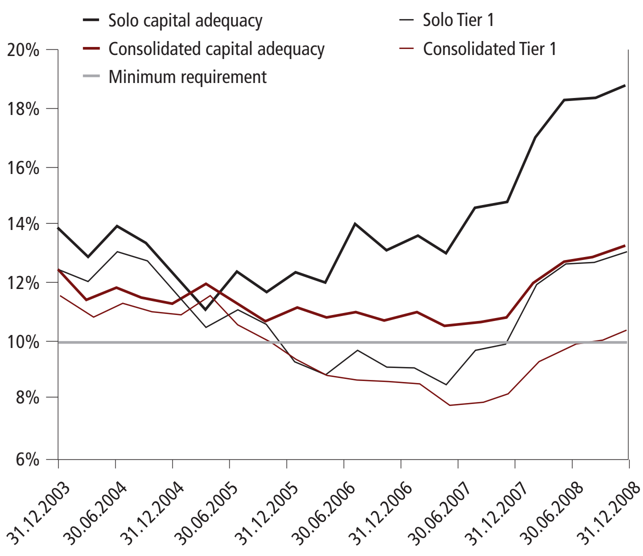
Figure 10. Quarterly bank revenues (in millions of kroons) and the cost-benefit ratio (rhs)



Strong capitalization of banks

As at 31 December 2008, the composite capital adequacy of banks on a solo basis was 18.82% (14.78% in 2007). Consolidated capital adequacy of banking groups was 13.32% at the end of 2008 (10.84% in 2007). Also so-called Tier 1 capital[11] remained on an adequate level both on solo and consolidated basis: Tier 1 capital was on a solo basis 13.08% and on a consolidated basis 10.40% at the end of 2008. Credit risk is still the major risk for the banking sector.

Figure 11. Capital adequacy of banks



[11] The share of Tier 1 own funds in the capital requirements. Tier 1 own funds are provided in Article 73(1) of the Credit Institutions Act.

6.3. Insurance companies

In 2008, eight non-life insurance companies, five life insurance companies and the Estonian Traffic Insurance Fund providing cross-border insurance and reinsurance were operating on the Estonian insurance market. Furthermore, five foreign insurers offered non-life insurance services through their local branches. A total of 313 providers of non-life insurance services and 80 providers of life insurance services have been entered in the register of providers of cross-border services in Estonia.

Insurance companies collected premiums within the amount of 5.8 billion kroons and paid claims to policyholders within the amount of 3.7 billion kroons in 2008. The drop in stock markets and the economic recession affected more the life insurance sector. The volume of insurance premium collected by Estonian life insurers decreased by 29.7% in 2008, while the volume of premiums collected by non-life insurers increased by 2.9%. The decline in the volume of insurance premiums was primarily caused by the drop in the popularity of unit-linked life insurance. Since the second half of 2008, we can notice the gradual shrinking of non-life insurance market.

Change in the ownership of insurance companies

QBE Kindlustuse Eesti AS terminated its insurance activities in 2008. It transferred its insurance portfolio to the Estonian branch of the QBE Insurance (Europe) Limited (belonging to the same group) as of 1 November 2008.

Also the ownership of life insurance company Seesam Life Insurance SE was changed. Its previous owner Suomi Mutual Life Assurance Company sold 100% of shares to Wiener Städtische Versicherung AG Vienna Insurance Group.

In 2008, two non-life insurers and one life insurer increased their stock capital. Changes in insurers' stock capital, the number of insurers and ownership structure had no effect on the share of non-residents' direct holdings in stock capital. Their total holding remained unchanged: 71%. Based on 2008 insurance premiums, non-residents controlled directly 65% of the market, including 77% of non-life insurance market and 43% of life insurance market. The rest of life insurance market (57%) was controlled by Estonian insurance companies owned by Estonia's two major banks which are directly controlled by Swedish investors.

Two non-life insurers opened branches in Baltic countries

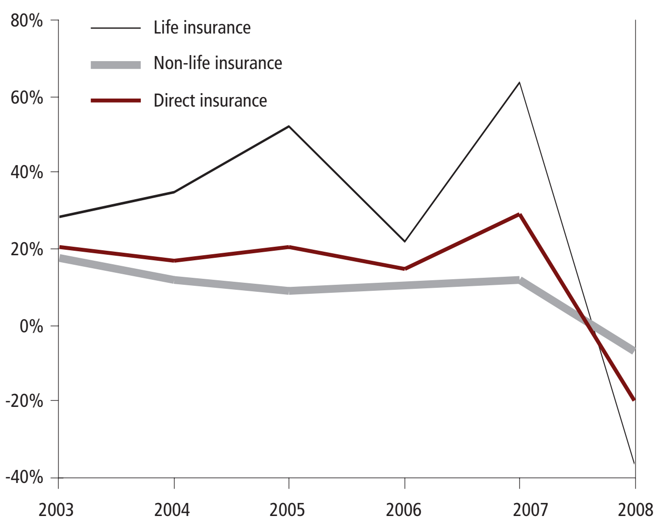
Two insurance companies extended their activities to encompass neighboring countries in order to find new policyholders. In 2008, the Financial Supervision Authority granted a permission to Swedbank Varakindlustus AS (AS Hansa Varakindlustus until 17 March 2009) to open a branch in Latvia, and to AS IF Eesti Kindlustus to open branches in Latvia and Lithuania.

Share of non-life insurance sector increased

During the year, the market distribution of direct insurance – life and non-life insurance – shifted by 9% in favor of non-life insurance. The share of non-life insurance increased to 65.9%. Considering the 10.4% increase in the consumer price index in 2008, the positive real growth of 29.2% in direct insurance in 2007 was reversed and it became negative in 2008. The real growth was -19.5% in 2008 *(See Figure 12)*.

The role of Estonia's insurance companies as reinsurers is still insignificant.

Figure 12. Real growth in insurance premiums, 2003–2008



6.3.1. Life insurers

In 2008, life insurers collected 1.98 billion kroons in insurance premiums, indicating a decrease of 29.7%. Contractual claims (including surrenders) of 1.4 billion kroons were paid out. Almost a third of insurance premiums were collected by Latvian and Lithuanian branches of Estonian life insurers.

Sale of unit-linked life insurance dropped

Policyholders have become extremely cautious due to the decline on global financial markets and the uncertainty about the future of Estonia's economy. The sale of unit-linked life insurance decreased 47.6% in 2008. While the premium volume of traditional life insurance contracts[12] increased 15.2%, part of this increase was due to the establishment of the European company Seesam Life Insurance SE at the end of 2007 leading to the inclusion of data of the company's Latvian and Lithuanian branches to the company's portfolio.

As at the end of 2008, Estonia's life insurers had 293,179 main contracts and 187,372 supplementary insurance contracts in force, totaling[13] 75.8 billion kroons; annuities amounted to about 0.9 billion kroons. Annual increase was 9.6% for main contracts and 6.7% for supplementary insurance contracts.

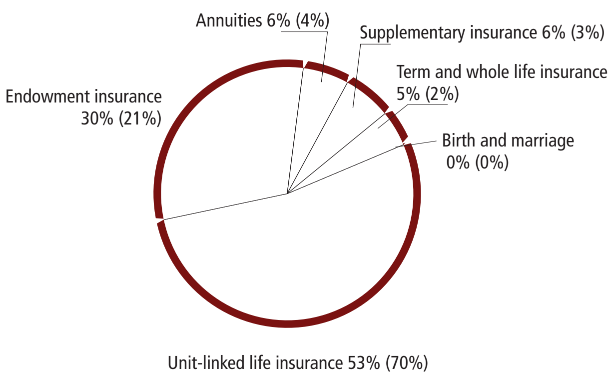
Based on the number of contracts, the most popular class of insurance was, as before, the endowment insurance which share in the number of main contracts in force at the end of 2008 was 40.3%. The share of endowment insurance contracts has been gradually decreasing over the last few years. Concurrently, the share of unit-linked insurance contracts has been increasing. Although the sale of unit-linked insurance contracts experienced a huge setback in 2008, the share of these contracts in the number of main contracts increased from 29.2% to 31.4%.

Increasing sale of term and whole life insurance contracts

In 2008, the volume of insurance premiums increased in all insurance classes, except birth and marriage insurance and unit-linked life insurance. The biggest share of new main contracts signed in 2008 formed term and whole life insurance contracts, constituting 43.4% of all new main contracts sold during the year.

Based on the volume of premiums, the most popular class of insurance was still unit-linked life insurance as unit-linked life insurance policies are generally characterized by larger than average premium payments per contract. Nevertheless, the share of premiums decreased from 71.4% to 53.2% in 2008 *(See Figure 13)*.

Figure 13. Structure of life insurance market in 2008 based on insurance premiums, in brackets 2007



12 Term and whole life insurance, endowment insurance, birth and marriage insurance and annuities.

13 The maximum amount of the sum insured paid out during the year (does not include amounts paid out as annuity payments).

Three major life insurers collected 82% of insurance premiums

The drop in the sale of unit-linked life insurance affected mostly the position of SE Sampo Life Insurance Baltic which was specialized on unit-linked insurance. Its share dropped by 11% in 2008 reaching 25%. Market share of Seesam Life Insurance SE increased from 5% to 14% due to the establishment of the European company. Market is still led by Swedbank Elukindlustus AS (AS Hansa Elukindlustus until 17 March 2009) *(See Figure 14).*

Insurance premiums collected by Swedbank Elukindlustus AS, AS SEB Elu- ja Pensionikindlustus and SE Sampo Life Insurance Baltic formed 82% of all insurance premiums.

Huge loss in life insurance sector

Based on unaudited data, four insurers out of total five had a loss in 2008. Total unaudited technical loss of life insurers was 310.6 million kroons and net loss was 297.1 million kroons (134.4 million kroons of profit in 2007). Loss in 2008 was primarily caused by the loss from investment activities amounting to 317.3 million kroons *(See Figure 15)*. In the second half of 2008, insurers were actively engaged in reviewing their investments in order to avoid further decline. Investments into short-term deposits increased considerably in 2008. Financial markets have to get more stable before insurers decide to make new investments into securities.

Figure 14. Market shares of life insurers by insurance premiums in 2008, in brackets 2007

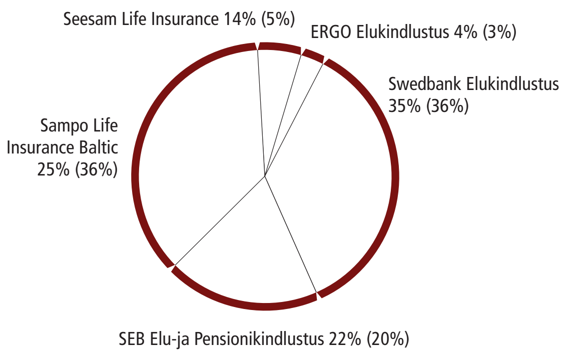
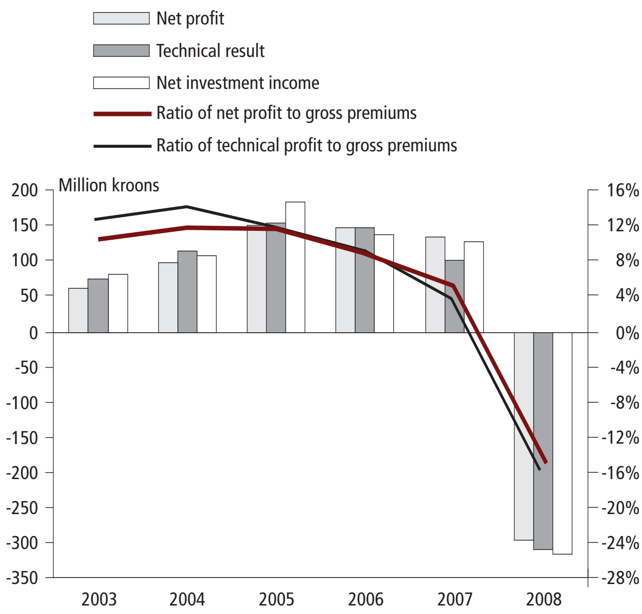


Figure 15. Profit (technical profit) and profit margin (technical profit margin) in life insurance sector, 2003–2008



6.3.2. Non-life insurers

Annual decrease of 27% in the assets of life insurers

Total assets of life insurance companies decreased by 26.8% and reached 6.2 billion kroons during the year. Commitments of insurers to policyholders, i.e. technical provisions and guaranteed financial commitments increased 4.4% during the year and reached 3 billion kroons by the end of the year. Investment volume of unit-linked insurance dropped from 4.5 billion kroons to 2.3 billion kroons due to the decline on financial markets as well as surrenders. The composite balance sheet of life insurers included investments in the amount of 3.7 billion kroons. All insurance companies complied with the requirements for committed assets and own funds provided by the Insurance Activities Act.

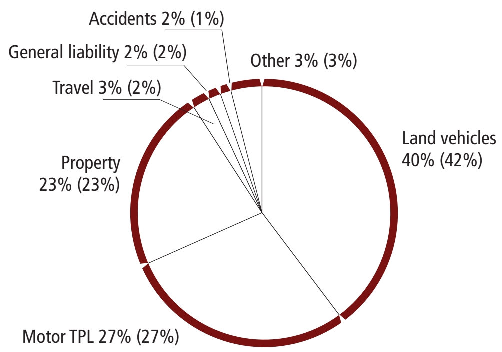
In 2008, the volume of gross premiums in non-life insurance amounted to 3.8 billion kroons, increasing 3% during the year (19% in 2007). The growth of premium volume slowed down considerably in the second half of the year and the last quarter witnessed even a slight decline – premiums were collected 6% less than in the fourth quarter of 2007. Claims paid amounted to 2.2 billion kroons, i.e. 7% more than in 2007.

Decreasing volume of land vehicle insurance premiums

The non-life insurance market was as before dominated by insurance classes related to motor vehicles. The volume of land vehicle insurance and motor TPL insurance formed 2/3 of the total market volume. Property insurance was the third largest insurance class. Shares of other classes remained within the range of 1% to 3% *(See Figure 16).*

Premium volume decreased in land vehicles insurance and commercial property insurance by about 1% and increased in motor TPL insurance by 3%. While the growth of insurance market has been primarily based on the requirement to insure vehicles and dwellings acquired by loan or lease, it is reasonable understandable that the growth slows down in a situation where the real estate market slows down and both the sale and leasing of new cars drop.

Figure 16. Non-life insurance portfolio structure by direct insurance premiums in 2008, in brackets 2007



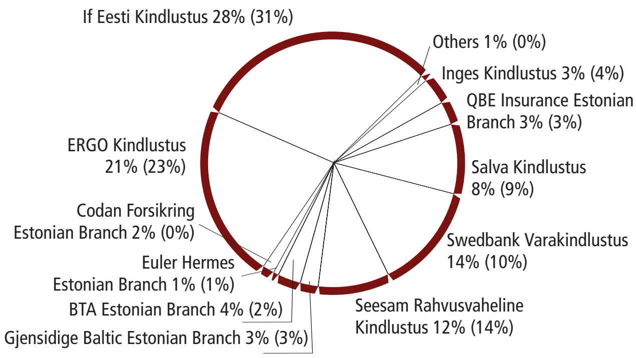
Increased competition by foreign branches

Non-life insurers authorized and operating in Estonia are experiencing stronger competition backed by local branches of foreign non-life insurance companies. Based on aggregate data of companies and branches, the volume of insurance premiums increased in total 8% in 2008, i.e. by 5% more than the growth calculated only on the basis of companies' data. The strongest competitors were primarily BTA apdrošinâšanas akciju sabiedrîba Estonian Branch, AAS Gjensidige Baltic Estonian Branch, and also Codan Forsikring A/S Estonian Branch which commenced its activities at the end of 2007.

Three major non-life insurers captured 63% of non-life insurance market

In 2008, significant changes took place in the market distribution. AS If Eesti Kindlustus maintained its leading position on the market, though its market share decreased by 3% in 2008. Non-life insurance market was redistributed and the winners were Swedbank Varakindlustus AS and branches of foreign insurance companies. Swedbank Varakindlustus AS increased its market share from 10% to 14% in a year, catching up with and passing by Seesam Rahvusvaheline Kindlustuse AS that had been on the third place in 2007. Branches of foreign insurers formed remarkable 11% of the total market volume in 2008 (6% in 2007). Market share controlled by three major life insurers was 63% at the end of 2008 and it had not remarkable changed since the end of 2007 *(See Figure 17)*.

Figure 17. Market shares of non-life insurers in 2008, in brackets 2007



Ceded reinsurance share in gross premiums decreased

In 2008, the share of ceded reinsurance in premium volume decreased to 12% in comparison with 14% in 2007. According to data of 2008, the share of ceded reinsurance in premium volume varied from 4% to 60%, depending on the company.

Loss from motor TPL insurance decreased

Year 2008 was more profitable for non-life insurers than the previous year and this is reflected in various ratios that characterize the insurance business of companies. Net loss ratio[14] was smaller in almost all non-life insurers. Main reason behind this decline was motor TPL insurance where the respective ratio decreased by approximately 24% in comparison with the previous year (both gross and net figures). Loss ratio of land vehicles insurance remained on the same level as in 2007 but in property insurance the loss ratio increased. The gross ratio of non-life insurance was 61.1% in 2008 (63.8% in 2007); net loss ratio was 61.5% (66% in 2007).

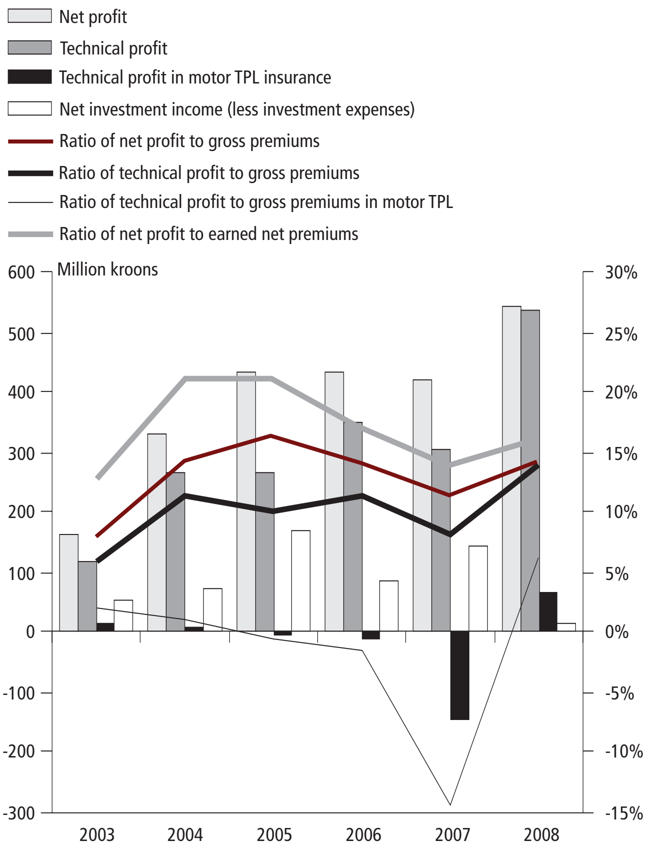
Increasing competition has forced non-life insurers to be more effective. In 2008, gross and net expense ratios[15] of non-life insurers were 21.7% and 22.4%, respectively. Both these ratios were approximately 1% smaller than in 2007.

The gross combined ratio[16] for non-life insurance companies was 82.9% in 2008 and the net combined ratio characterizing the profitability of insurers themselves was 83.9%, both being smaller than the respective figures for 2007.

Net profit increased more than 25%

Year 2008 was profitable for non-life insurance sector[17]: investment profit totaled 16 million kroons, technical profit 536 million kroons and net profit 539 million kroons. The result was the worst in the fourth quarter due to the financial crisis; still, the total result was positive. More than great technical result compensated the poor net investment income. Based on 2008 data, net profit of non-life insurers increased 28%. Year 2008 was ended with net profit by all insurers but one *(See Figure 18).*

Figure 18. Profit (technical profit) and profit margin (technical profit margin) for non-life insurers, 2003-2008



[14] Ratio of claims incurred to earned premiums (gross figure includes reinsurance).
[15] Ratio of administrative expenses and deferred acquisition costs to earned premiums.
[16] Combined ratio = loss ratio + expense ratio (gross figure includes reinsurance).
[17] Unaudited data.

Growth of 10% in the assets of non-life insurance companies

The asset volume of non-life insurance companies reached to 5.4 billion kroons at the end of 2008. Technical provisions for non-life insurance companies (net of reinsurance) stayed on the level of 2007 and totaled 2.1 billion kroons, forming 38.6% of the balance sheet volume. The total volume of investments and cash and cash equivalents on the aggregated balance sheet of non-life insurers was 4.7 billion kroons. At the end of 2008, all non-life insurance companies complied with the requirements for committed assets and own funds provided by the Insurance Activities Act.

6.4. Insurance intermediaries

As at 31 December 2008, the list of insurance intermediaries included 26 Estonian insurance brokers, about 600 cross-border insurance brokers, and about 1100 cross-border insurance agents who are entitled to provide insurance brokerage services on the Estonian market.

While the gross premium volume of insurance contracts mediated by brokers increased both in 2006 and 2007 by 20–35% on an average and the growth in the volume of brokerage (commission fees) was between 20% and 50% for most of the brokers, year 2008 witnessed the slowdown in this growth. Gross premium volume of insurance contracts mediated in 2008 increased 2–10%, in single cases also more, in comparison with 2007.

Most of the biggest and most experienced insurance brokers registered in Estonia are members of Estonian Insurance Brokers Association and most of them achieved the same sales volume in 2008 as in the previous year. Single brokers could even improve their results.

In 2008, the volume of brokerage fees (incl. contracts sold in previous years) that non-life insurance companies paid was about 170.5 million kroons. About 1.8 million kroons was paid to insurance brokers from other countries.

Insurance brokers are rarely used in life insurance. In 2007, the volume of brokerage fees that life insurance companies paid to Estonian insurance brokers was about 296 thousand kroons. About 360 million kroons was paid to insurance brokers from other countries.

The number of notices received from EU member countries in respect of the mediation of cross-border insurance services is constantly increasing; still, the activities of cross-border insurance intermediaries have currently no significant effect on the Estonian insurance mediation market. The number of insurance contracts mediated from foreign countries will probably increase in areas where it is complicated to find the respective insurance product from the local insurance market.

Due to the economic recession, year 2009 can be expected to witness a decrease in the number and volume of mediated insurance contracts caused by the decrease in the total volume of sold insurance contracts. Current economic situation sets higher standards for insurance brokers in respect of proper adherence to legal rules.

6.5. Fund management companies and funds

6.5.1. Fund management companies

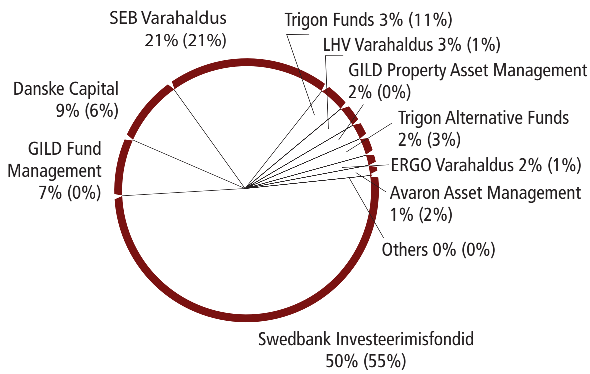
As at 31 December 1008, there were 14 locally authorized fund management companies operating in Estonia.

Three new fund management companies entered the market in 2008: AS Limestone Investment Management, Nordea Pensions Estonia AS and AS Redgate Asset Management (former AS Redgate Varahaldus). AS Limestone Investment Management offers its services to funds registered in Luxembourg and Nordea Pensions Estonia AS focuses on the management of pension funds. AS Redgate Asset Management, who acquired the license at the end of the year, was not able to commence its activities in 2008. AS GILD Property Assets Management and AS GILD Fund Management, who acquired their licenses in 2007, commenced their activities in offering fund units in 2008.

Good year for pension fund management companies

Considerable decrease in the volume of equity funds lead to the redistribution of market between fund management companies in 2008. The following fund management companies engaged primarily in the management of pensions funds were in a more favorable position: Danske Capital AS, AS LHV Varahaldus, ERGO Funds AS and Nordea Pensions Estonia AS *(See Figure 19).* In addition, a very good position was captured by AS GILD Fund Management who is the manager of a new hedge fund and AS GILD Property Asset Management who is the manager of a real estate fund. Market share of these two fund management companies formed 9% of the market at the end of 2008. The market share of AS Trigon Funds who is specialized on equity funds decreased from 11% to 3%. The reason behind the decreasing market share of Swedbank Investeerimisfondid AS (market leader) was high percentage of equity funds in the total volume of funds managed by it.

Figure 19. Market shares of fund management companies, based on investment funds' volume, 31.12.2008 (in brackets 31.12.2007)



Concentration on the fund market was still high, despite the redistribution of market. At the end of 2008, the three largest fund management companies controlled 80% of the market (82% in 2007).

Total volume of managed assets decreased significantly

Total assets managed by fund management companies decreased in 2008 from 41.7 billion kroons to 27.8 billion kroons, of which 21.3 billion kroons originated from managed investment funds and 6.5 billion kroons from clients' securities portfolios. The volume of securities portfolios experienced no major change in 2008. Portfolio management services were offered by five fund management companies.

6.5.2. Investment and pension funds

Asset volume of fund management companies grew by 12%

Total asset volume of fund management companies reached 1.4 billion kroons by the end of 2008 and there were no significant changes in the structure of assets. As at 31 December 2008, the highest share in the aggregated balance sheet was captured by the item 'Receivables from credit institutions' with 46%. The second major share belonged to investments into managed funds, forming approximately 24% of the balance sheet volume at the end of 2008.

Profits of the sector decreased by threefold

Based on unaudited data, fund management companies received a profit of 101 million kroons in 2008 (72% less than in 2007). Despite the global financial crisis, more than half of fund management companies ended the year with a profit. Profits of the sector were mostly decreased by the decline in management fees and unrealized losses from long-term financial investments. Decline in securities markets jeopardized more such fund management companies which are more exposed to market risk. The main source of market risk proved to be voluntary investments into managed investment funds other than pension funds and investments into securities.

Total amount of administrative expenses of fund management companies sector increased approximately 36% in 2008. This growth was mainly caused by start-up costs of new fund management companies. The total amount of administrative expenses of older fund management companies actually decreased.

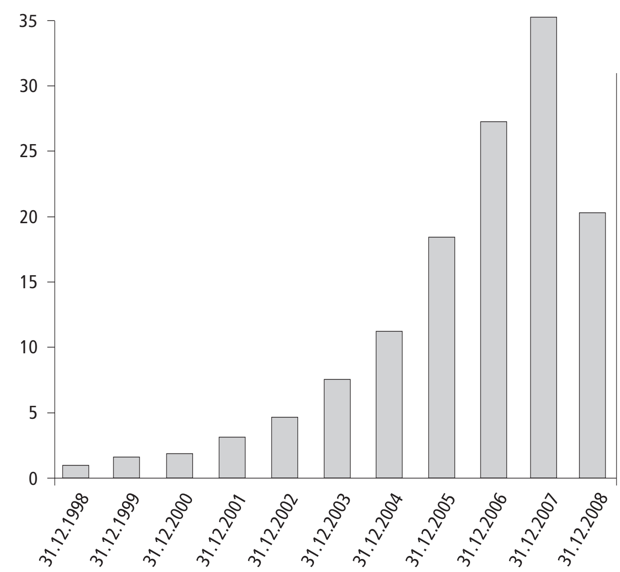
Financial crisis cut the profitability of equity capital and the profitability of 2008 was 8% (37% in 2007).

Own funds of the fund management sector exceeded the solvency margin requirement by 324% at the end of 2008 (219% in 2007). Surplus varies significantly among fund management companies. The growth in surplus was backed up by the profit earned in 2007, most of which was not distributed as dividends.

The net asset value of investment funds (including pension funds) decreased by 40% (i.e. 14 billion kroons) in 2008, reaching 20.6 billion kroons by the end of the year. Such an asset volume is comparable with the volume in the middle of 2006 *(See Figure 20).*

Developments of 2008 in global financial markets had a significant effect on the Estonian fund sector. Due to the decline in investment values also the asset volume of investment and pension funds decreased considerably, leading to negative performance of funds and thus also to the decline in the value of units belonging to unit-holders. The volume of finds decreased because of the decrease in investment values and the trend of investors exiting the funds.

Figure 20. Dynamics of the net asset value of investment funds (incl. pension funds) for 1998–2008 (in billions of kroons)



While the aggregate asset volume of funds decreased by 3.6 billion kroons in January, it still remained relatively stable for seven months, amounting to 31–32 billion kroons. As a result of a drop in stock markets triggered by the bankruptcy of the US investment bank Lehman Brothers in September, the aggregate asset volume of funds decreased by 11.1 billion kroons during the last four months of the year, whereas the biggest drop occurred in October (6.4 billion kroons) *(see Figure 21)*.

Despite these difficult times on global financial markets and low spirits of investors, several new investment and pension funds were registered in Estonia in 2008. The number of registered investment funds increased from 58 to 76 in 2008. 1 debt fund, 3 equity funds, 4 mandatory pension funds, 5 voluntary pension funds, 3 real estate funds and 2 hedge funds entered the market in 2008. Their net asset value totaled 2.5 billion kroons as at 31 December 2008, forming 12% of total assets of investment and pension funds. The entrance of new funds compensated in a certain extent the decline in 2008.

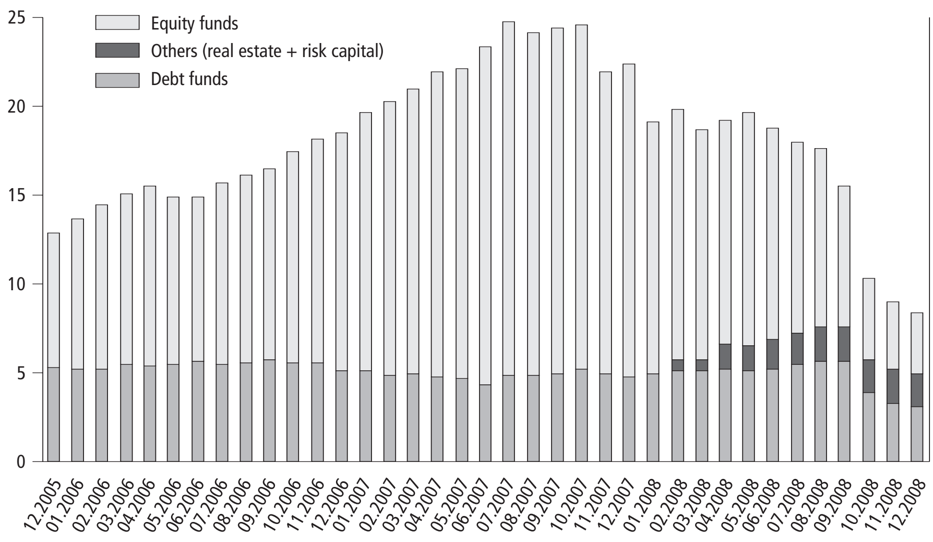
Asset volume of equity funds decreased

Year 2008 proved to be a very tough year for equity funds which had been experiencing a long growth phase. The asset volume of equity funds registered in Estonia decreased from 17.7 billion kroons at the beginning of the year to the final 3.5 billion kroons, thus the drop being 80%. The asset volume of equity funds had been on such a low level at the end of 2004. The number of unit-holders totaled 25,647 at the end of 2008.

The asset volume of debt funds, money market funds and interest funds decreased 36%, totaling 3.1 billion kroons at the end of 2008.The number of unit-holders decreased to 4,452 by the end of 2008.

The asset volume of other types of funds that had entered the Estonian market in 2008 – i.e. real estate funds, risk capital funds and hedge funds – totals 1.8 billion kroons at the end of 2008 and the number of unit-holders reached to 603.

Figure 21: Asset volume of investment funds (in billions of kroons)



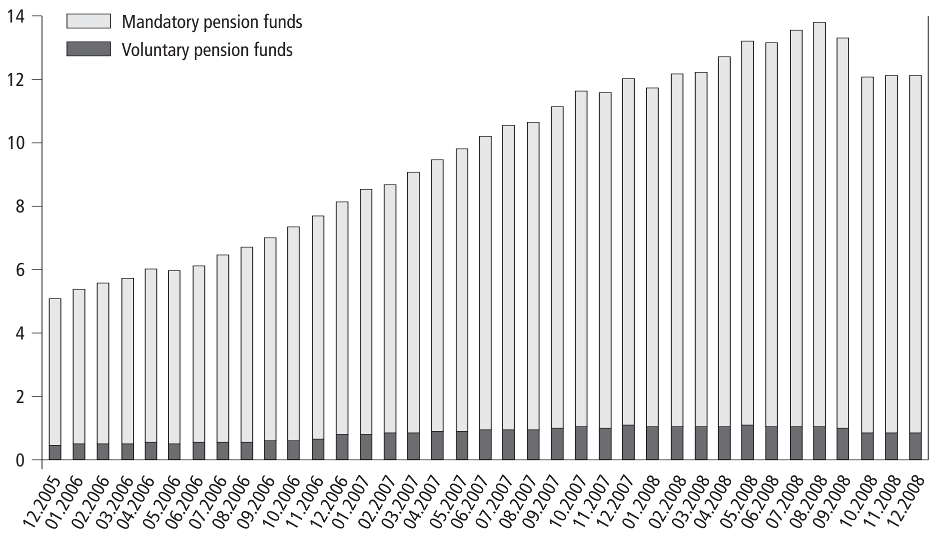
Decrease in asset volume of pension funds

The growth in the asset volume of Estonian pension funds slowed down during the first eight months of 2008 as compared to previous periods. While the average increase in the asset volume of mandatory pension funds was 300 million kroons per month, first eight months of 2008 witnessed an average growth of 225 million kroons per month. Still, the situation changed dramatically during the subsequent months. In despite of regular payments made by those who had joined the pension system, the total asset volume of mandatory pension funds decreased finally by 1.5 billion kroons, mostly due to equity investments that had lost their value.

Consequently, contrary to previous years the asset volume of mandatory pension funds remained virtually unchanged during the year, the annual growth being only 3% (0.38 billion kroons), totaling 11.4 billion kroons at the end of 2008 *(See Figure 22)*. The number of joined persons of mandatory pension funds reached to 580,046 at the end of the year.

The asset volume of voluntary pension funds decreased 27% (0.3 billion kroons) in 2008, totaling 0.8 billion kroons at the end of the year. The number of unit-holders was 53,031 at the end of 2008.

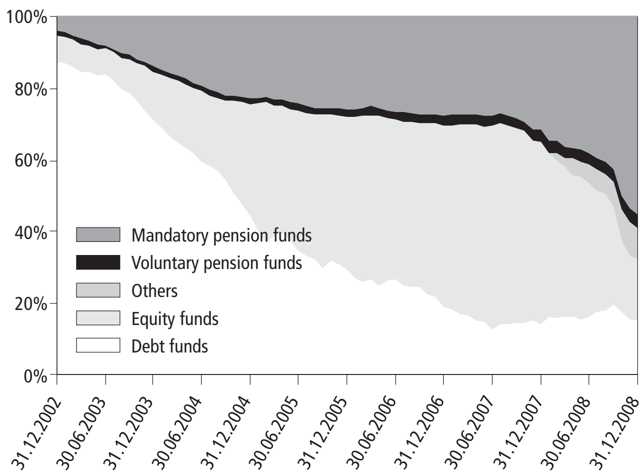
Figure 22. Asset volume of pension funds (in billions of kroons)



Change in the market structure of funds

In 2008, the structure of Estonian fund market which had been relatively stable in recent years changed considerably. The share of so far dominating equity funds decreased from 51% to 17%. The share of mandatory pension funds increased from 32% to 55% and thus became the biggest fund type in the Estonian fund sector. The share of debt funds increased from 14% to 15% of the total market volume. The share of voluntary pension funds increased from 3% to 4%. Other funds totaled 9% of the total market volume *(See Figure 23)*.

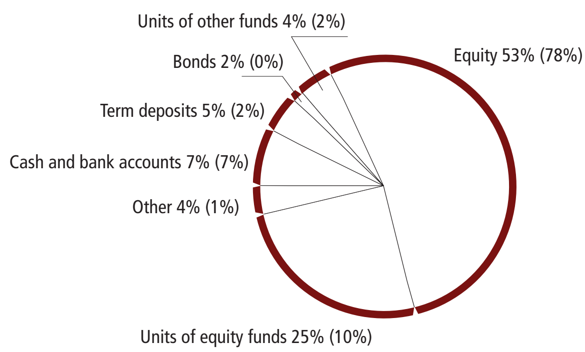
Figure 23. Division of market between different fund types, 31.12.2002–31.12.2008



Share of equity investments dropped

Situation on equity markets lead to the change in the structure of funds' investments. The share of equity investments decreased from 88% to 78% of the aggregate investment portfolio of equity funds. Direct equity investments decreased from 78% to 53%. Investments into other equity funds increased from 10% to 25% *(See Figure 24)*.

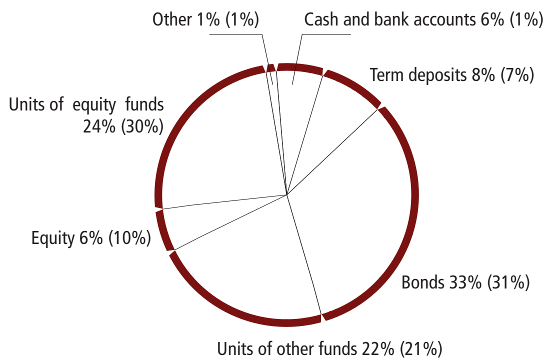
Figure 24. Asset structure of equity funds, 31.12.2008 (in brackets 31.12.2007)



The share of interest-bearing instruments – i.e. investments into debt securities and deposits – has increased.

The share of equity investments has also decreased in mandatory pension funds – from 40% to 30%. Direct equity investments decreased from 10% to 6% and investments into other equity funds decreased from 30% to 24% *(See Figure 25)*.

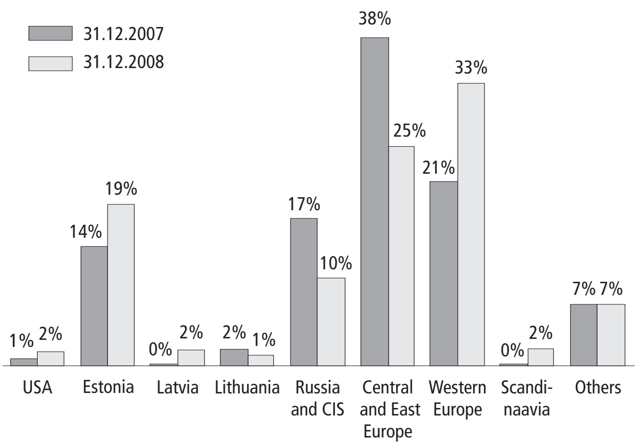
Figure 25. Asset structure of mandatory pension funds as at 31.12.2008 (in brackets 31.12.2007)



Geographical shift toward developed markets

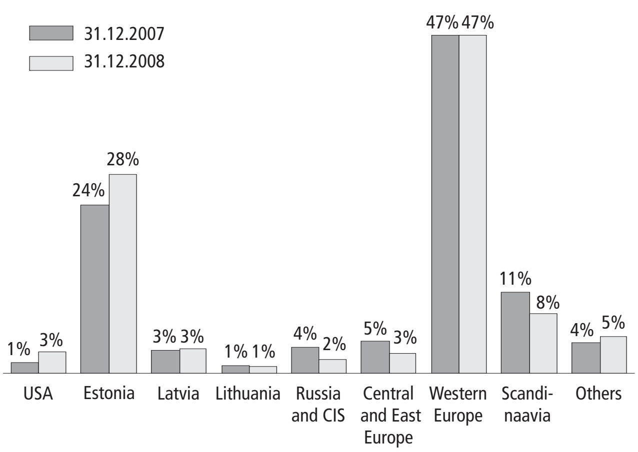
There has been a shift in geographical distribution of equity funds' investments from Central and East European markets towards Western Europe. The share of issuers registered in Central and East Europe decreased from 38% to 25% in 2008. The share of issuers from Western Europe increased from 21% to 33% *(See Figure 26)*.

Figure 26. Geographical distribution of equity funds' investments



Changes were smaller in geographical distribution of mandatory pension funds' investments as these funds had been more prudent in choosing investments. Still, we can notice the drop in the share of developing countries: the share of Russia and CIS decreased from 4% to 2% and the share of Central and East Europe decreased from 5% to 3% *(See Figure 27)*.

Figure 27. Geographical distribution of mandatory pension funds' investments

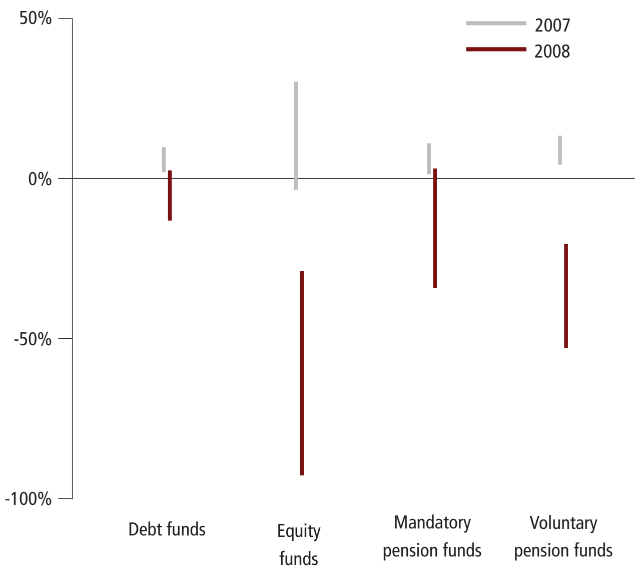


Negative performance of most of the funds

Out of funds registered in Estonia, the positive performance was achieved only by SEB Konservatiivne Pensionifond (+3%), Kohustuslik Pensionifond Sampo Pension Intress (+2%), Sampo Likviidsusfond (+2%) and ERGO Pensionifond 2P1 (former Rahulik Pensionifond +2%) in 2008.

Global financial crisis had the most dramatic effect on equity funds whose performance in 2008 was between -93% and -29%, whereas in case of 18 equity funds the unit value dropped twice or more. Performance of debt funds was between -13% and +2%, that of mandatory pension funds between -34% and +3% and voluntary pension funds between -53% and -20%.

Figure 28. Annual performance range of various fund types



6.6. Investment firms

In 2008, there were 7 investment firms authorized and operating in Estonia. The number of investment firms remained the same during the year. Also a branch of a foreign investment firm – the Estonian Branch on the Finnish investment firm Privanet Pankkiiriliike Privanet – was operating in Estonia.

Changing market shares

Based on the sales volume of investment services, the leading position on the market was captured by AS GILD Financial Advisory Services, who could stay in competition and capture over 50% of sector's turnover both on markets of financial advisory services and asset management despite the decline in market demand. Market shares were increased also by AS LHV Varahaldus and AS KIT Finance Europe who were less affected by the decline in demand. Market shares of Evli Securities AS and AS SEB Enskilda decreased considerably. The latter was highly affected by the low level of corporate finance advisory services market *(See Figure 29)*.

Figure 29. Market shares of investment firms by the sales volume of investment services, 2008 (in brackets 2007)

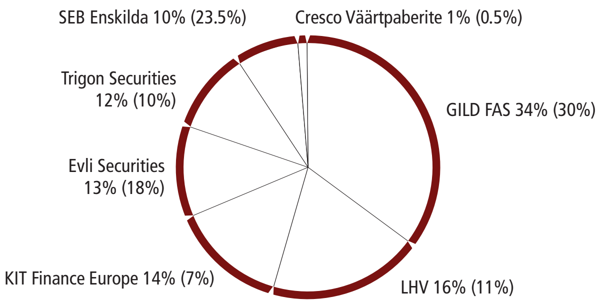


Figure 30. Advisory services

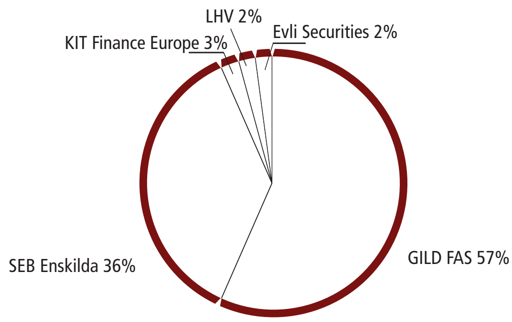


Figure 31. Securities brokerage

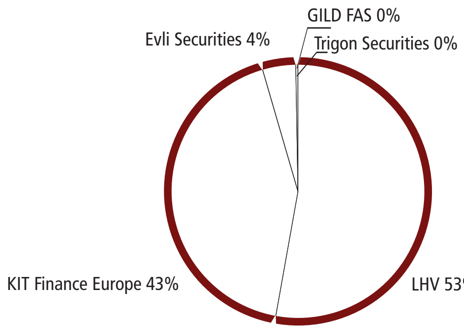
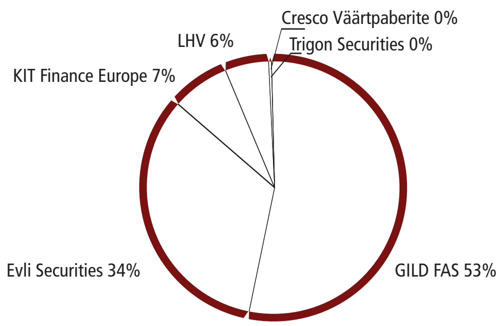
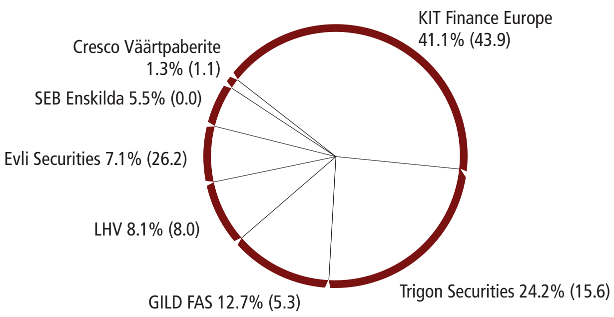


Figure 32. Portfolio and asset management



AS KIT Finance Europe, the subsidiary of a Russian investment bank was as before the largest investment firm by asset volume *(See Figure 33).*

Figure 33. Market shares of investment firms by asset volume, 31.12.2008 (in brackets 31.12.2007)

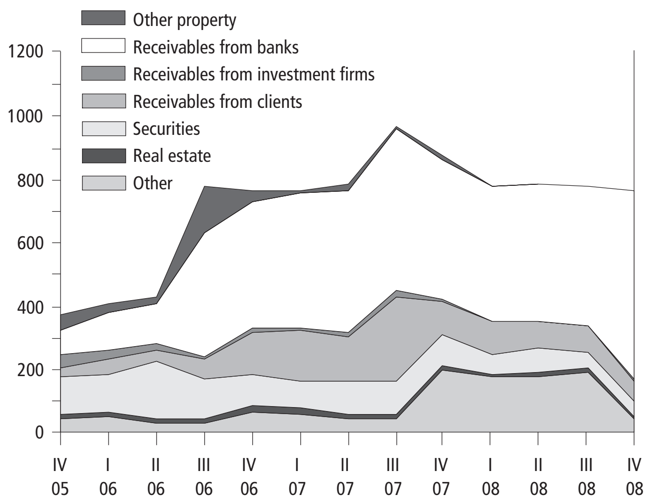


Low level of balance sheet risks

The volume and structure of assets changed considerably during the year. Asset volume of investment firms remained within the range of 800 million kroons and thus the investment firms' sector is the smallest sector supervised by the Financial Supervision Authority. Investment firms drew income primarily from the sale of mediation and advisory services which do not require the acceptance of major balance sheet risks. Thus, the asset volume of investment firms remained moderate *(See Figure 34).*

None of the investment firms had a noteworthy actively managed trading portfolio. Securities formed only 9% of assets in 2008 (12.5% in 2007). Several investment firms granted short-term loans backed by securities to clients, mostly as leverage for short-term securities investments of clients. Due to smaller demand for leveraged investments, loans granted to clients decreased from 11% to 6% in 2008.

Figure 34. Aggregate assets of investment firms (in millions of kroons)



Drop in incomes and profits

Profits of investment firms dropped dramatically in comparison with 2007. Profitability of the sector decreased all together 75% in 2008 *(see Figure 35)*. The reason behind such a decline was the poor sales of investment services. Investment firms earned from the sale of investment services 289 million kroons, i.e. one third less than in the last year (426 million kroons in 2007). The second reason behind the decline was the increase of 30% in administrative expenses *(see Figure 36)*.

All investment firms experienced a significant decrease in profitability, but a huge loss was earned by only one investment firm; the rest of the sector earned practically no profit or received positive profit. The next year is expected to witness even bigger drop in income from service fees. Still, the positive effect may come from cost-saving measures adopted by most of the companies.

Adequate capital buffers

Regulative own funds of the sector exceeded the capital requirement established for investment firms by 9 times, i.e. the sector as an average was considerably overcapitalized *(see Figure 37)*. Nevertheless, in case of single unprofitable investment firms we can speak about an inadequacy of potential own funds. The Financial Supervision Authority monitored closely these investment firms. Other investment firms were at least satisfactorily capitalized. There was no direct threat to proper performance of the requirement as most of investment firms did not earn huge losses.

Figure 35. Profit and Return on Equity (ROE) of investment firms (in millions of kroons)

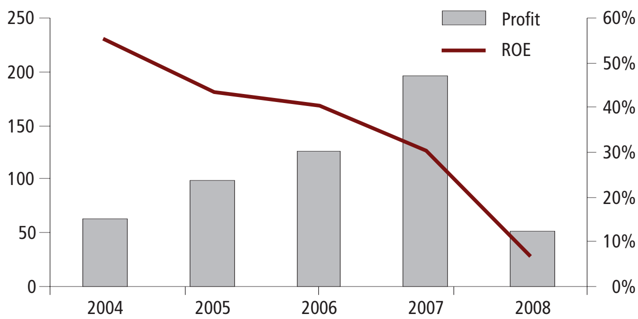


Figure 36. Revenues of investment firms by areas of activity (in million of kroons)

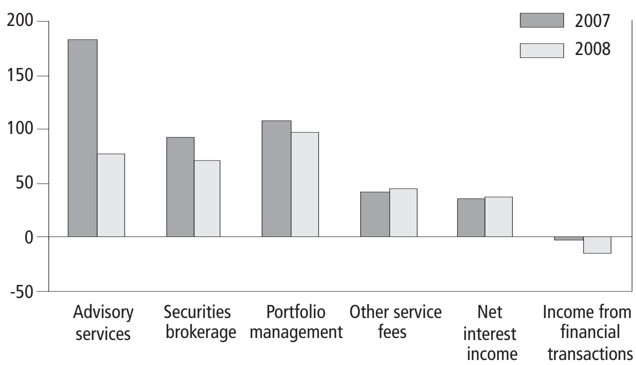
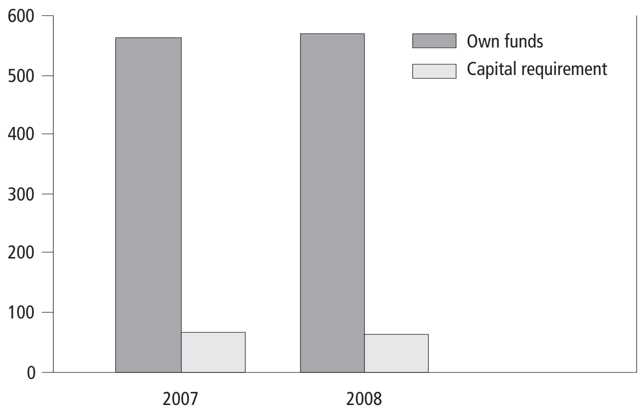


Figure 37. Aggregate own funds and capital requirement of investment firms (in millions of kroons)



6.7. Investment services

6.7.1. Management of securities portfolios

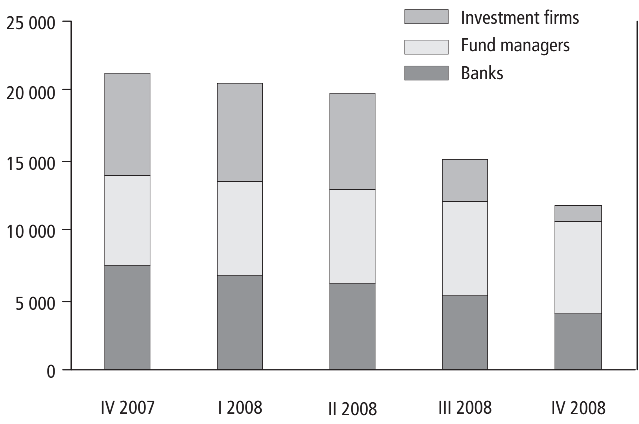
Management of securities portfolios is the management of portfolios made up of securities offered to each individual client separately according to general directions given by the client. Securities portfolio management service can be provided by fund management companies, investment firms and credit institutions.

The volume of portfolios managed by companies that are supervised by the Financial Supervision Authority totaled 12 billion kroons at the end of 2008 (21 billion kroons in 2007). The annual decrease in the volume of managed portfolios was 45% *(see Figure 38)*. This decline in the value of clients' investment portfolios was the biggest in the sector of investment firms where the portfolio management of several major professional investors had been transferred out of Estonia.

This decline in clients' investment portfolios was probably caused by the drop on global stock markets which was especially big in case of Central and East European markets. Losses earned on stock markets forced many clients to review their investment strategies and to transfer their funds into safer instruments in order to avoid further losses.

The decline in clients' securities portfolios will probably not reverse until trends in Central and East European economies turn around and expectations of investors for the prospects of this region become more positive again.

Figure 38. Management of securities portfolios by sectors (in millions of kroons)



6.7.2. Safekeeping of securities

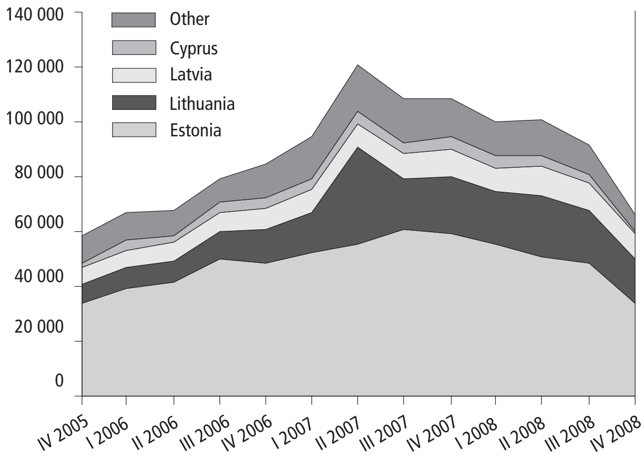
Safekeeping of securities means the safekeeping of securities on securities account opened in the name of a credit institution or an investment firm by third parties or in the Central Register of Securities in a way that third parties cannot identify the ultimate owner of securities. Pursuant to legislation in force in Estonia and in many EU countries, securities kept for clients are separated from the bankruptcy estate of service provider.

More than 90% of securities belong to professional investors: other banks, insurers, funds, government, etc.

Banks kept in total 66 billion kroons of clients' securities at the end of 2008. The annual decrease in the volume of kept securities was 40% *(see Figure 39)*.The value of shares and units of investment funds has dropped the most. Significant drop in the volume of clients' investments was caused by the decrease in securities' market values triggered by the decline in securities markets, and by clients' wish to liquidate more risky investments.

Investment firms kept in total 1.7 billion kroons of clients' securities at the end of 2008 (2.9 billion kroons in 2007).

Figure 39. Securities kept in banks by countries of location (in millions of kroons)

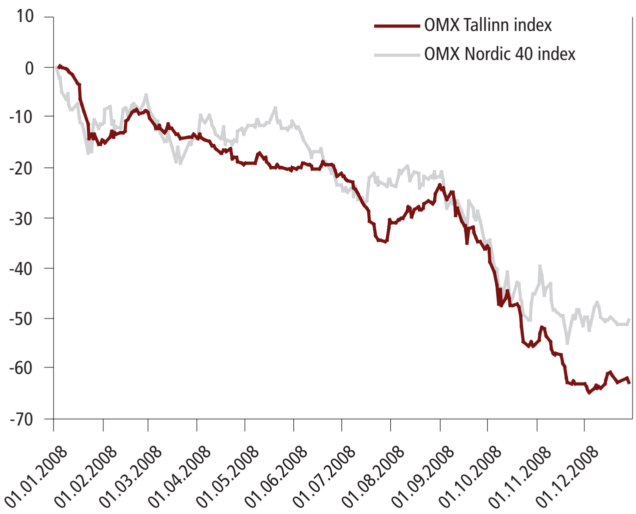


6.8. Issuers

Both at the beginning and at the end of 2008, there were shares of 18 companies altogether allowed to be traded on NASDAQ OMX Tallinn Stock Exchange which is the only regulated securities market in Estonia. The list of debt issuers formerly including five companies was extended by one more company. There were no initial public offerings during 2008. This can be explained by the severe drop in stock prices in 2008 that affected all property types and regions and lead to unprecedented correction in stock prices of companies listed on NASDAQ OMX Tallinn Stock Exchange.

The general trend in the prices of the shares listed on NASDAQ OMX Tallinn Stock Exchange is reflected by the OMX Tallinn index which achieved the highest level of 1043 points in eleven years of activity of Tallinn Stock Exchange in February 2007. On 31th of December 2007, the index closed at 742 points. The decline in stock prices continued in 2008 and the index decreased to 275 point by the end of the year, the drop being 63%. In comparison with OMX Nordic 40 encompassing 40 major Nordic companies, the decline in OMX Tallinn index was 13% steeper; nevertheless, this small difference shows effectively that also very big securities markets were affected by the decline and that the drop in NASDAQ OMX Tallinn Securities Exchange was no exception *(see Figure 40)*.

Figure 40. Change in OMX Tallinn and OMX Nordic 40 indices in 2008 (%)



Delisting of the shares of AS Saku Õlletehas

All issuers continued their day to day business activities despite the negative change in their stock prices. Moreover Carlsberg Breweries A/S, 100% subsidiary of Carlsberg A/S acquired the remaining 50% of the shares of Baltic Beverages Holding AB on 9th of May 2008. Consequently, Saku Õlletehase AS was controlled by Carlsberg A/S and approximately 92.4% of shares of Saku Õlletehas belonged to Carlsberg A/S after the compulsory takeover bid. Based on the results of compulsory takeover bid, Carlsberg A/S decided to commence activities for taking over the shares belonging to other minority shareholders. These actions lead to the delisting of the shares of Saku Õlletehas from the main list of NASDAQ OMX Tallinn Stock Exchange on 20th of September 2008.

6.9. Securities market operators

6.9.1. NASDAQ OMX Tallinn

Restructuring of AS Merko Ehitus

On 14th of March 2008, AS Merko Ehitus notified of its plan to separate its everyday commercial activities from the criminal case related to the exchange of parcels. Management of the company made a proposal to shareholders for restructuring the group and notified the investors of its wish to suspend the trading with shares of AS Merko Ehitus until the publication of its restructuring plan. NASDAQ OMX Tallinn Stock Exchange declined the application as it considered that the long-term suspension of trading only because of the disclosure of restructuring plans is not in line with the interests of investors. As a result of restructuring AS Merko Ehitus, the company was renamed to AS Järvevana and all its assets, liabilities and contracts were handed over to a new company which started to operate under the name of AS Merko Ehitus and which shares were introduced on the stock exchange on 11th of August 2008.

Transaction between AS Kalev and Alta Capital Partners S.C.A cancelled

On 31 March 2008, AS Kalev and AS Alta Foods (controlled 100% by Alta Capital Partners S.C.A) signed the memorandum concluded on 20 September 2007 for the sale of AS Kalev's shares in its subsidiaries AS Kalev Chocolate Factory, AS Kalev Jõhvi Tootmine, AS Kalev Paide Tootmine, AS Valmetek Invest, AS Vilma and OÜ Maiasmokk. The buyer had to pay 660 million kroons by 30th of May 2008 at the latest for these shares, but the purchase price was not paid by Alta Capital Partners S.C.A by the deadline and thus the seller did not hand over the shares.

Listing of debt securities of OÜ Manutent

NASDAQ OMX Tallinn Stock Exchange Listing and Supervision Committee decided to decline to list the debt securities of OÜ Manutent in order to protect the investors. This decision was based on the company's economic situation, market position, area of activity and other circumstances. After OÜ Manutent had complied with additional terms, it was decided to list 7000 debt securities of OÜ Manutent totaling 110 million kroons.

NASDAQ OMX Tallinn Stock Exchange is the only regulated secondary market for securities in Estonia, providing the administration of the environment necessary for trading with securities, matching of transaction orders, settlement of transactions with securities and listing of companies.

Owners of Tallinn Stock Exchange and new business name

In 2008, NASDAQ and OMX merged and created the world's biggest stock exchange group. Consequently, also the business name of Tallinn Stock Exchange was changed to NASDAQ OMX as of December 2008. The stock exchange group launched in September the trading environment NASDAQ OMX Europe based on NASDAQ OMX technology platform and at the end of 2008 all information communication services of Nordic and Baltic stock exchanges were united under the brand name GlobeNewswire. Year 2009 is expected to witness real-time information on prices of shares listed on NASDAQ OMX Baltic stock exchanges and the extension of trading periods of Baltic stock exchanges by two hours.

Baltic stock exchanges, including NASDAQ OMX Tallinn Stock Exchange received new members in 2008: Instinet LLC (UK), UAB Finhill (Lithuania), SEB AB (Sweden), AB bankas Finasta (Lithuania), Evli Bank plc (Finland) and the new pan-Baltic member AB Ukio bankas (Lithuania). Membership was cancelled by Nordnet (Sweden) and Evli Securities AS (Estonia). Baltic stock exchanges had 42 members at the end of 2008.

The most active broker – Swedbank AS

Swedbank AS was the most active member on NASDAQ OMX Tallinn Stock Exchange in 2008 and its trading accounted for almost 46% of the total turnover of the stock exchange and little more than 37% of the total number of transactions. It was followed by AS SEB Pank with 34% and 20%, respectively, and the third place was taken by Evli Securities AS with 7% and 5%, respectively *(See Figure 41).*

Steep drop in market value of publicly traded companies

Market value of shares of companies publicly traded on NASDAQ OMX Tallinn Stock Exchange was 64.2 billion kroons at the beginning of 2008 and 22 billion kroons at the end of 2008, the drop being 66% *(See Figure 42).*

Figure 41. Participation of Stock Exchange members in total turnover, 2008

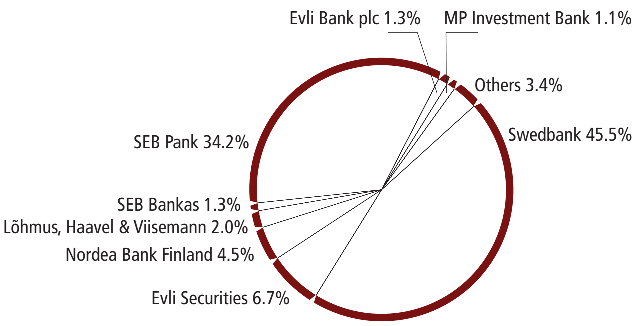
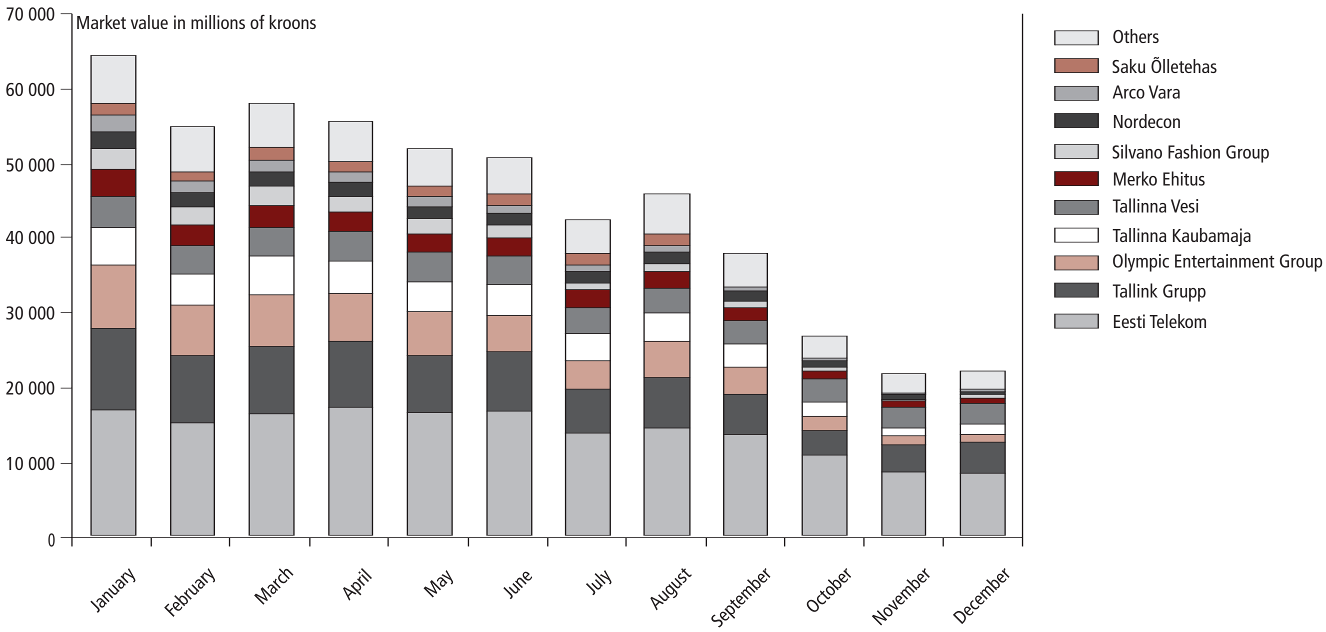


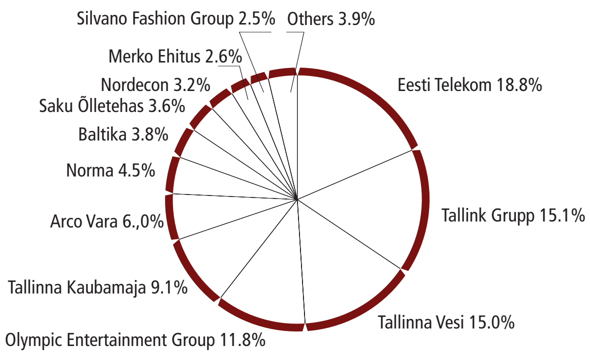
Figure 42. Market value of securities traded on NASDAQ OMX Tallinn Stock Exchange, 2008



Significant decrease in Stock Exchange turnover

Turnover of NASDAQ OMX Tallinn Stock Exchange decreased 60% in comparison with 2007, totaling 77,265 transactions with the value of about 9.7 billion kroons. An average value of a stock exchange transaction was a little more than 125,000 kroons. In 2008, trading was most active with the shares of AS Eesti Telekom; they were followed by the shares of AS Tallink Grupp and AS Tallinna Vesi *(see Figure 43)*.

Figure 43. Structure of securities' turnover, 2008



Also intra-Baltic trading slowed down and the number of transactions decreased almost by one third in comparison with 2007. The number of cross-border securities' transactions concluded between Estonia, Latvia and Lithuania totaled 69,470. In addition, 132 transactions were concluded between Estonia and Poland. Estonian Central Register of Securities and Polish Central Securities Depository had signed a cooperation agreement in July 2007.

One of the primary indicators of market liquidity – the ratio of turnover and average market capitalization – on NASDAQ OMX Tallinn Stock Exchange was 35.4% in 2007 and this ratio decreased to 22.4% in 2008. There were 77,265 transactions with shares and bonds made on the Stock Exchange. The decline was more than 45% in comparison with 2007.

6.9.2. Estonian Central Register of Securities

The Estonian Central Register of Securities (initially called the Estonian Central Securities Depository), founded in 1994, is the central electronic register of Estonian securities and the administrator of the register for pension funds in Estonia, and it keeps accounts of all the securities accounts and pension accounts opened in Estonia and the share registers of all public limited companies operating in Estonia. It also administers the acceptance of applications for the funded pension or II pillar of the pension system, and the issuance of fund units. The Estonian Central Register of Securities in the infrastructure company of securities market belonging to the international NASDAQ OMX group and owned by NASDAQ OMX Tallinn AS.

There were 131,228 valid securities accounts registered with the Estonian Central Register of Securities at the end of 2008 (annual growth of 5%). There were about 24,000 active investors who had made at least five transactions (stock exchange transactions + over-the-counter transactions), i.e. 1000 accounts less than in 2007. The number of empty accounts remained quite stable in 2008, but experiencing a slight increase during the last months of the year.

Annex I. Organisational structure of the Financial Supervision authority

SUPERVISORY BOARD

MANAGEMENT BOARD

Raul Malmstein
Chairman of the Management Board

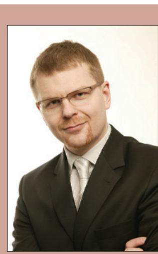
- Head of Communications
- Head of Human Resources
- Internal Auditor
- Coordinator of International Cooperation
- Consumer Education Specialist
- Assistant to the Chairman

Andres Kurgpõld
Member of the Management Board

- Prudential Supervision Division
- Prudential Policy and Financial Reporting Division

Kaido Tropp
Member of the Management Board

- Business Conduct Supervision Division
- Administrative Services Department



Kilvar Kessler
Member of the Management Board

- Market Supervision and Enforcement Division
- Legal Department

Annex 2. List of Supervised Entities as of December 31 2008

Supervised entities	Address	Contact		Executive Director
Credit institutions				
AB Bankas Snoras Estonian Branch	Roosikrantsi 17, 10119 Tallinn	www.snoras.com	6 272 971	Raivo Sulg
Allied Irish Banks PLC Estonian Branch	Roosikrantsi 11, 10119 Tallinn	www.amcredit.ee	6 277 180	Jeffrey Gawley
AS Eesti Krediidipank	Narva mnt 4, 15014 Tallinn	www.krediidipank.ee	6 690 900	Andrus Kluge
AS Parex banka Estonian Branch	Roosikrantsi 2, 10119 Tallinn	www.parex.ee	7 700 000	Sofia Krist
AS SEB Pank	Tornimäe 2, 15010 Tallinn	www.seb.ee	6 655 100	Ahti Asmann
AS UniCredit Bank Estonian Branch	Liivalaia 13/15, 10118 Tallinn	www.unicreditbank.ee	6 688 300	Taavi Laur
Bank DnB NORD A/S Estonian Branch	Tartu mnt 10, 10145 Tallinn	www.dnbnord.ee	6 868 500	Hans Pajoma
BIGBANK AS	Rüütli 23, 51006 Tartu	www.bigbank.ee	7 377 570	Targo Raus
Danske Bank A/S Estonian Branch	Narva mnt 11, 15015 Tallinn	www.sampopank.ee	6 800 800	Aivar Rehe
Marfin Pank Eesti AS	Pärnu mnt 12, 10148 Tallinn	www.marfinbank.ee	6 802 500	Riho Rasmann
Nordea Bank Finland PLC Estonian Branch	Hobujaama 4, 15068 Tallinn	www.nordea.ee	6 283 300	Vahur Kraft
Pohjola Bank plc Estonian Branch	Pärnu mnt 141, 11314 Tallinn	www.pohjola.fi	6 630 840	Arja Helena Jurmu
Scania Finans AB Estonian Branch	Peterburi tee 72, 11415 Tallinn	www.scania.ee	6 651 263	Veljo Barbo
Svenska Handelsbanken AB Estonian Branch	Harju 6, Tallinn 10130	www.handelsbanken.se	6 808 300	Rauno Klettenberg
Swedbank AS	Liivalaia 8, 15040 Tallinn	www.swedbank.ee	6 310 310	Håkan Berg
Tallinna Äripanga AS	Vana-Viru 7, 10111 Tallinn	www.tbb.ee	6 688 000	Valeri Haritonov
AS DnB NORD Banka Estonian Branch (in liquidation)	Tartu mnt 10, 10145 Tallinn	www.dnbnord.ee	6 868 500	Hans Pajoma, Kairi Evard, Andis Paulins (liquidators)
Siemens Financial Services AB Estonian Branch (in liquidation)	Pärnu mnt 139C, 11317 Tallinn	www.siemens.ee	6 305 705	Jarl Anders Stenbock (liquidator)

Supervised entities	Address	Contact		Executive Director
Life insurers				
ERGO Elukindlustuse AS	Lauteri 5, 10114 Tallinn	www.ergo-kindlustus.ee	6 106 677	Kęstutis Bagdonavičius
AS Hansa Elukindlustus	Liivalaia 12, 15036 Tallinn	www.hansa.ee/elukindlustus	6 131 120	Mihkel Mandre
SE Sampo Life Insurance Baltic	Jõe tn 3, 10151 Tallinn	www.sampolife.ee	6 812 300	Imre Madison
Seesam Life Insurance SE	Roosikrantsi 11, 10119 Tallinn	www.seesamlife.ee	6 103 000	Olga Reznik
AS SEB Elu- ja Pensionikindlustus	Tornimäe 2, 10145 Tallinn	www.seb.ee	6 656 840	Indrek Holst
Non-life insurers				
D.A.S. Õigusabikulude Kindlustuse AS	Veerenni 58A, 11314 Tallinn	www.das.ee	6 799 450	Maiko Kalvet
ERGO Kindlustuse AS	A. Lauteri 5, 10114 Tallinn	www.ergo-kindlustus.ee	6 106 500	Kęstutis Bagdonavičius
AS If Eesti Kindlustus	Pronksi tn 19, 10124 Tallinn	www.if.ee	6 671 100	Andres Sooniste
AS Inges Kindlustus	Raua 35, 10124 Tallinn	www.inges.ee	6 410 436	Voldemar Vaino
Salva Kindlustuse AS	Pärnu mnt 16, 10141 Tallinn	www.salva.ee	6 800 500	Tiit Pahapill
Seesam Rahvusvaheline Kindlustuse AS	Vambola 6, 10114 Tallinn	www.seesam.ee	6 281 801	Ivo Kuldmäe
Swedbank Varakindlustus AS	Liivalaia 12, 15039 Tallinn	http://www.swedbank.ee/ /varakindlustus	8 882 100	Margus Liigand
MTÜ Eesti Liikluskindlustuse Fond	Mustamäe tee 44, 10621 Tallinn	www.lkf.ee	6 671 800	Kristjan Niinemaa
Fennia Mutual Insurance Company Estonian Branch	Harju 6, 10130 Tallinn	www.fennia.fi	6 310 691	Kalmet Kala
Euler Hermes Kreditversicherungs-Aktiengellschaft Estonian Branch	Pirita tee 20, 10127 Tallinn	www.eulerhermes.ee	6 028 105	Frank Wille
BTA Apdrošināšanas akciju sabiedrība Estonian Branch	Lootsi 3a, 10151 Tallinn	www.bta-kindlustus.ee	6 868 060	Lauris Boss
Codan Forsikring AS Estonian Branch	Peterburi tee 2f, 11415 Tallinn	www.royalsunalliance.ee	6 224 557	Kaido Kepp
AAS Gjensidige Baltic Estonian Branch	Sõpruse pst 145, 13417 Tallinn	www.gjensidige.ee	6 755 380	Marko Privoi
QBE Insurance (Europe) Limited Estonian Branch	Sõpruse pst 145, 13417 Tallinn	www.qbeeurope.com/ estonia	6 671 400	Aivar Vähi

Supervised entities	Address	Contact		Executive Director
Insurance brokers				
AAA Kindlustusmaakler OÜ	Narva mnt 4–420			Artur Karaman
Aadel Kindlustusmaaklerid OÜ	Laki 11 12915 Tallinn	www.aadel.ee	6 816 910	Tõnis Laks
OÜ ABC Kindlustusmaaklerid	Endla 69/Keemia 4, 10615	www.kindlustuseabc.ee	6 679 650	Erik Sei
AS AON Eesti Kindlustusmaakler	Liivalaia 13/15, 10118 Tallinn	www.aon.com	6 996 227	Lauri Tõnise
BCP Kindlustusmaakler OÜ	Narva mnt 9A, 10117 Tallinn	www.kindlusmaaklerid.ee	6 616 844	Janek Järva
Colemont Kindlustusmaakler OÜ	Peterburi tee 2f, 11415 Tallinn	www.colemont.ee	6 679 130	Heiki Nurmeots
CHB Kindlustusmaakler OÜ	Mustamäe tee 24, 10621 Tallinn	www.chb.ee	6 650 160	Andry Saarm
Clemenc Kindlustusmaakler OÜ	Punane 6–203, 13619 Tallinn		6 213 065	Elina Skljarova
Credo Kindlustusmaakler OÜ	Mäepealse 21a, 12618 Tallinn	www.credokindlustus.ee	6 829 696	
Fix-Kindlustus Kindlustusmaakler OÜ	Kaarna 32, 10620 Tallinn		5 500 004	Gerli Toomla
IIZI Kindlustusmaakler AS	Tartu mnt 2, 10145 Tallinn	www.iizi.net	6 660 300	Risto Rossar
AS In Bro & Partners Kindlustusmaakler	Tartu mnt 87d, 10112 Tallinn	www.inbro.ee	6 115 240	Markus Haiba
KindlustusEst Kindlustusmaakler OÜ	Mustamäe tee 55, 10621 Tallinn	www.kindlustusest.ee	6 678 683	Maldon Ots
K. Kindlustusmaakler OÜ	Narva mnt 90, 10127 Tallinn	www.kindlustusjuht.ee	6 022 025	Reet Lahesalu
Kominsur Kindlustusmaakler OÜ	Mooni 18, 10613 Tallinn	www.kominsur.ee	6 616 970	Dmitri Soljanik
Krooni Kindlustusmaaklerid OÜ	Pikk 11, 80010 Pärnu	www.kroonivara.ee	4 423 001	Eve Põldemaa
Lõuna Kindlustusmaakler OÜ	Raatuse 20, 51009 Tartu		7 407 134	Andro Ross
OÜ Marks ja Partnerid Kindlustusmaaklerid	Endla 69/Keemia 4, 10615 Tallinn	www.marks.ee	6 680 266	Jaan Marks
Marsh Kindlustusmaakler AS	Tartu mnt 18, 10115 Tallinn	www.marsh.ee	6 811 000	Mart Mere
Optimal Kindustusmaakler OÜ	Nõmme tee 59/2, 11311 Tallinn	www.optimal.ee	6 562 828	Tarmo Hillep
AS Smart Kindlustusmaakler	Lõõtsa 2B, 11415 Tallinn	www.smartkindlustus.ee	6 181 610	Heiki Puusaar
AS SEB Kindlustusmaakler	Tornimäe 2, 10145, Tallinn	www.seb.ee	6 549 677	Raivo Piibor
OÜ Kindlustusmaakler Tiina Naur	Juhkentali 52, 10132 Tallinn	www.naur.ee	6 420 022	Tiina Naur
Vagner RE Kindlustusmaakler OÜ	Villardi 23–2, 10136 Tallinn		6 312 627	Roman Illarionov
Vagner Kindlustusmaakler AS	Villardi 23–2, 10136 Tallinn	www.vagner.ee	6 312 627	Roman Illarionov
AS Vandeni Kindlustusmaaklerid	Tornimäe 7 PO Box 149 10145 Tallinn	www.vanden.ee	6 164 550	Raul Källo

Supervised entities	Address	Contact		Executive Director
Fund management companies and funds				
AS Avaron Asset Management	Narva mnt 5–58, 10117 Tallinn	www.avaron.ee	6 644 205	Kristel-Kivinurm Priisalm
Avaron Areneva Euroopa Väikeettevõtete Fond				
Avaron Balkani Fond				
Avaron Valitud Aktsiate Fond				
Danske Capital AS	Narva mnt 9A, 10117 Tallinn	www.sampopank.ee	6 752 295	Silja Saar
Kohustuslik Pensionifond Sampo Pension 25				
Kohustuslik Pensionifond Sampo Pension 50				
Kohustuslik Pensionifond Sampo Pension Intress				
Vabatahtlik Pensionifond Sampo Pension 100 Pluss				
Vabatahtlik Pensionifond Sampo Pension Intress Pluss				
Danske Likviidsusfond				
Danske Invest Globaalne Kasvufond				
Danske PP Arenenud Turgude Aktsiastrateegia Fond				
Danske PP Arenevate Turgude Aktsiastrateegia Fond				
Danske PP Intressistrateegia Fond				
Danske Uus Euroopa Fond				
Ergo Funds AS	A. Lauteri 5, 10114 Tallinn	www.ergofondid.ee	6 106 500	Marek Zacek
Ergo Pensionifond 2P1 (former Rahulik Pensionifond)				
Ergo Pensionifond 2P2 (former Tuleviku Pensionifond)				
Ergo Pensionifond 3P1				
Ergo Pensionifond 3P2				
Ergo Pensionifond 3P3				
AS GILD Fund Management	Tartu mnt 2, Tallinn 10145	www.gildbankers.com	6 800 401	Tõnis Haavel
GILD Arbitrage Riskikapitalifond				

Supervised entities	Address	Contact		Executive Director
AS GILD Property Asset Management	Rävala pst 6, Tallinn 10143	www. gildrealestate.com	6 814 761	Urmas Laur
Eastern Europe Real Estate Investment Fund				
AS Kawe Kapital	Pärnu mnt 15, 10141 Tallinn	www.kawe.ee	6 651 704	Ago Lauri
Kawe Investeerimisfond				
AS LHV Varahaldus	Tartu mnt 2, 10145 Tallinn	www.lhv.ee	6 800 400	Mihkel Oja
LHV Täiendav Pensionifond				
Pensionifond LHV Uued Turud				
Pensionifond LHV Maailma Aktsiad				
Pensionifond LHV Tasakaalustatud Strateegia				
Pensionifond LHV Dünaamilised Võlakirjad				
Pensionifond LHV Kvaliteetsed Võlakirjad				
LHV Tõusva Euroopa Alfa Fond				
LHV Pärsia Lahe Fond				
LHV Maailma Aktsiad Fond				
AS Limestone Investment Management	Väike-Karja 12, 10140 Tallinn	www.limestonefunds.eu	7 120 801	Mihkel Õim
Nordea Pensions Estonia AS	Hobujaama 4, 15068 Tallinn	www.nordea.ee	6 283 300	Angelika Tagel
Nordea Pensionifond A				
Nordea Pensionifond B				
Nordea Pensionifond C				
Nordea Pensionifond Aktsiad 100				
AS Redgate Asset Management	Sõpruse pst 151, 13417 Tallinn	www.redgatecapital.eu	6 668 200	Veikko Maripuu
AS SEB Varahaldus	Tornimäe 2, 15010 Tallinn	www.seb.ee	6 655 100	Sven Kunsing
SEB Kasvufond				
SEB Geneerilise Farmaatsia Fond				
SEB Tasakaalukas Fondifond				
SEB Aktiivne Fondifond				
SEB Dünaamiline Fondifond				
SEB High Yield Bond Fund				
SEB Ida-Euroopa Võlakirjafond				
SEB Likviidsusfond				
SEB Konservatiivne Pensionifond				
SEB Optimaalne Pensionifond				

Supervised entities	Address	Contact		Executive Director
SEB Progressiivne Pensionifond				
SEB Aktiivne Pensionifond				
SEB Tasakaalukas Pensionifond				
Swedbank Investeerimisfondid AS	Liivalaia 8, 15038 Tallinn	www.swedbank.ee	6 310 310	Fabio Filipozzi
Swedbank Intressifond				
Swedbank Ida-Euroopa Aktsiafond				
Swedbank Ida-Euroopa Võlakirjafond				
Swedbank Rahaturufond				
Swedbank Venemaa Aktsiafond				
Swedbank Kesk-Aasia Aktsiafond				
Swedbank Ida-Euroopa Kinnisvara Aktsiafond				
Swedbank Private Debt Võlakirjafond				
Swedbank Fondifond 30				
Swedbank Fondifond 60				
Swedbank Fondifond 100				
Hansa GAM Diversity Fond (in liquidation)				
Hansa GAM Multi-Arbitrage Fond (in liquidation)				
Swedbank Pensionifond K1				
Swedbank Pensionifond K2				
Swedbank Pensionifond K3				
Swedbank Pensionifond V1				
Swedbank Pensionifond V2				
Swedbank Pensionifond V3				
AS Trigon Alternative Funds	Viru väljak 2, 10111 Tallinn	www.trigoncapital.com	6 679 200	Heiti Riisberg
Trigon Active Alpha Fund				
Trigon Adriatic Property Kinnisvarafond				
Trigon Ukrainian Property Kinnsivarafond				
AS Trigon Funds	Viru väljak 2, 10111 Tallinn	www.trigoncapital.com	6 679 200	Mehis Raud
Trigon Balkani Fond (former Trigon Teise Laine Fond)				
Trigon Uus Euroopa Väärtusfond (former Trigon Kesk- ja Ida-Euroopa Fond)				

Supervised entities	Address	Contact		Executive Director
Trigon Uus Euroopa Väikeettevõtete Fond				
Trigon Top 10 Fond				
Trigon Arenevate Turgude Finantssektori Fond				
Trigon Arenevate Turgude Põllumajandussektori Fond				
Investment companies				
AS GILD Financial Advisory Services	Tartu mnt 2, 10145 Tallinn	www.gildbankers.ee	6 800 401	Rain Tamm
AS KIT Finance Europe	Roosikrantsi 11, 10119 Tallinn	www.kitfinance.ee	6 676 270	Kaido Kaljulaid
AS Lõhmus, Haavel & Viisemann	Tartu mnt 2, 10145 Tallinn	www.lhv.ee	6 800 400	Erki Kilu
AS SEB Enskilda	Tornimäe 2, 15010 Tallinn	www.enskilda.ee	6 655 390	Henrik Igasta
AS Trigon Securities	Pärnu mnt 15, 10141 Tallinn	www.trigoncapital.com	6 679 200	Merle Keskel
Cresco Väärtpaberite AS	Tartu mnt 2, 10145 Tallinn	www.cresco.ee	6 405 880	Olev Schults
Evli Securities AS	Tartu mnt 2, 10145 Tallinn	www. evli.com	6 405 700	Aidas Galubickas
Privanet Pankkiiriliike Oy Estonian Branch	Videviku 1, 93815 Kuressaare	www.privanet.fi		Jaanika Merilo

FINANCIAL SUPERVISION AUTHORITY
Sakala 4
15030 TALLINN

Telephone: +372 668 0500
Fax: +372 668 0501
E-mail: info@fi.ee
Website: www.fi.ee

Beginning of financial year: 1 January 2008
End of financial year: 31 December 2008
Core activity: Financial supervision
Management Board: Raul Malmstein, Kilvar Kessler, Andres Kurgpõld, Kaido Tropp
Auditor: AS PricewaterhouseCoopers