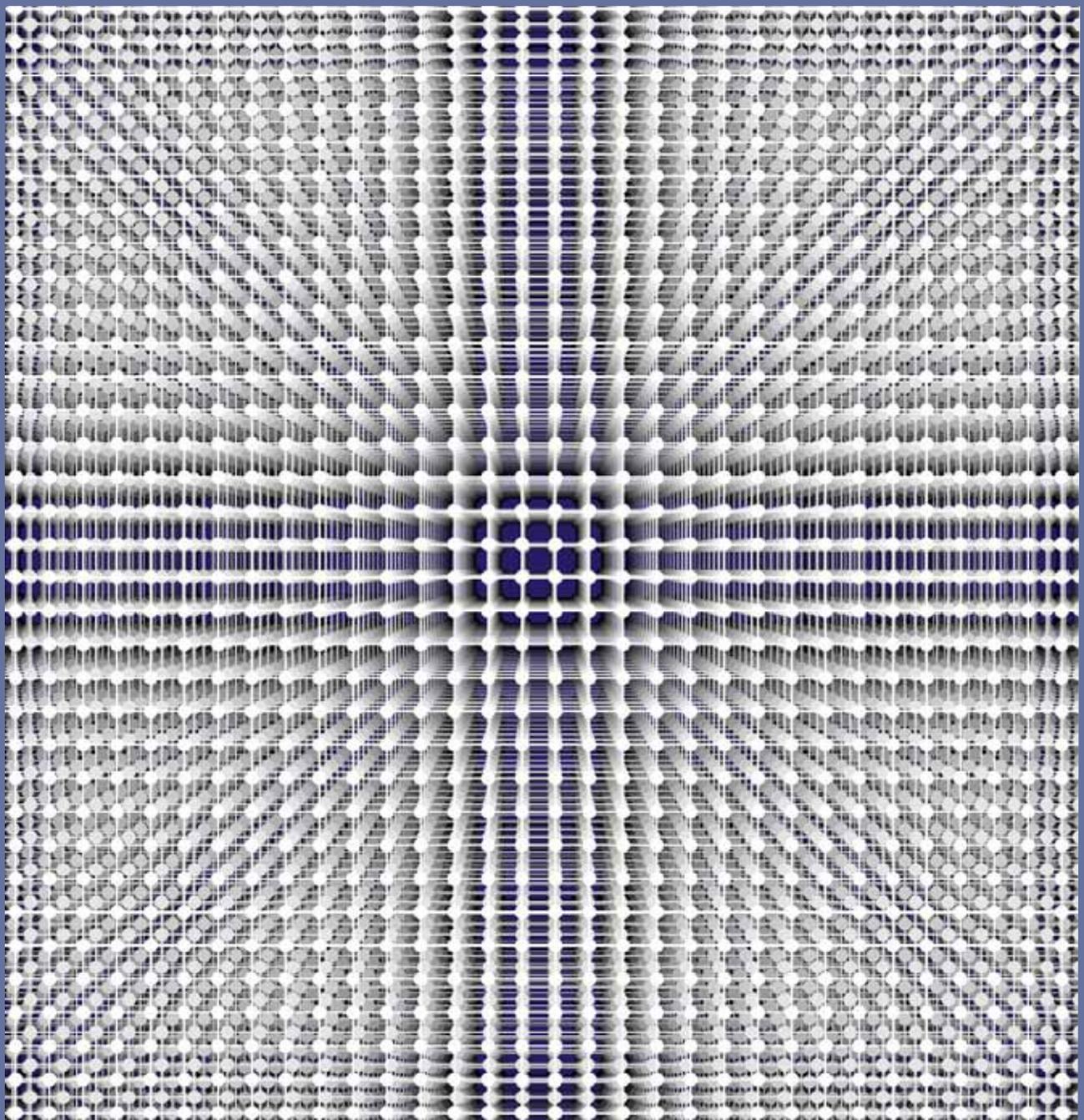


**PAYMENT AND SECURITIES SETTLEMENT SYSTEM OVERSIGHT  
CONDUCTED BY LATVIJAS BANKA IN 2013**



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## ABBREVIATIONS

ACBL – Association of Commercial Banks of Latvia  
 ATM – Automated Teller Machine  
 CPSS – Committee on Payment and Settlement Systems  
 CPSS-IOSCO – Committee on Payment and Settlement Systems and International Organisation of Securities Commissions  
 CRPC – Consumer Rights Protection Centre  
 CSD – Central Securities Depository  
 DENOS – securities settlement system of the LCD  
 DVP – delivery versus payment  
 EC – European Commission  
 ECB – European Central Bank  
 EKS – electronic clearing system of Latvijas Banka  
 e-money – electronic money  
 ESCB – European System of Central Banks  
 ESCB-CESR – ESCB and the Committee of European Securities Regulators (CESR<sup>1</sup>)  
 EU – European Union  
 FCMC – Financial and Capital Market Commission  
 FDL – local lats clearing and settlement system of FDL  
 FOP – free of payment  
 IT – information technologies  
 JSC – Joint Stock Company  
*Latvijas Pasts* – *SJSC Latvijas Pasts*  
 LCD – Latvian Central Depository  
 LDDK – Employers' Confederation of Latvia  
 LIKTA – Latvian Information and communications Technology Association  
 Ltd – Limited liability company  
 MPSWG – Money and Payment Systems Working Group of the Republic of Latvia  
 Euro Project Steering Committee  
 SMECCC – Small and Medium-Sized Enterprises and Crafts Consultative Committee  
 NSWG – National SEPA Working Group  
 OTC – over-the-counter  
 POS – Point of Sale  
 PNS – postal settlement system of *Latvijas Pasts*  
 RE – Register of Enterprises of the Republic of Latvia  
 r.i. – restricted information  
 SAMS – interbank automated payment system of Latvijas Banka  
 SEPA – Single Euro Payments Area  
 SJSC – State Joint Stock Company  
 SRS – State Revenue Service  
 SSIA – State Social Insurance Agency  
 Stock Exchange – Stock Exchange NASDAQ OMX Riga  
 TARGET – Trans-European Automated Real-time Gross settlement Express Transfer system  
 TARGET2 – second generation system of TARGET  
 T2S – TARGET2-Securities  
 US – United States of America

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<sup>1</sup> As of 1 January 2011, the European Securities and Markets Authority (ESMA).

## EXECUTIVE SUMMARY

In 2013, Latvijas Banka pursued activities to prepare for the introduction of the euro in Latvia and successful changeover of Latvijas Banka payment systems from the settlement in lats to the settlement in euro. Latvijas Banka performed data simulations of the SAMS and TARGET2-Latvija to assess liquidity adequacy in TARGET2-Latvija after the changeover to the euro.

Latvijas Banka conducted the compliance assessment of DENOS against the Eurosystem User Standards in cooperation with the Eurosystem to enable the use of DENOS and Latvia's securities registered with DENOS in the Eurosystem's monetary policy operations as of the changeover to the euro. DENOS was deemed to be eligible for the use in the Eurosystem's monetary policy operations and intraday credit operations as of 1 January 2014.

An assessment of the EKS compliance with the *Core Principles for Systemically Important Payment Systems* (hereinafter, the Core Principles) was performed in accordance with a time frame of Latvijas Banka activities under the Euro Project. Latvijas Banka carried out the relevant activities to prepare the EKS for the changeover to the euro, assessing the introduction of additional clearing cycles from the oversight perspective.

In 2013, Latvijas Banka conducted a day-to-day oversight of interbank payment systems SAMS, EKS, TARGET2-Latvija maintained by Latvijas Banka and also that of the securities settlement system DENOS maintained by the LCD, analysing technical and operational functions of the systems and compiling statistical data on these systems. In 2013, the daily average of payments processed via all three payment systems maintained by Latvijas Banka totalled 140.0 thousand payments with the value of 936.5 million lats. In 2013, the SAMS processed 235.0 thousand payments with the value of 125.6 billion lats (the daily average – 936 payments with the value of 500.5 million lats); TARGET2-Latvija handled 349.8 thousand payments with the value of 132.0 billion euro (92.7 billion lats; the daily average – 1 372 payments with the value of 517.5 million euro or 363.7 million lats) and EKS processed 34.6 million payments with the value of 18.2 billion lats (the daily average – 137.7 thousand payments with the value of 72.3 million lats). The availability of the SAMS and TARGET2 totalled 100.00%, while the availability of the EKS accounted for 99.83% (the delays in settlement exceeded 30 minutes only on three occasions out of 1 715 over the year). The analysis of systemic risk suggested that risk still remained low. The total volume of financial instruments transfers executed via DENOS stood at 42.7 thousand in 2013, of them, DVP accounted for 23.5 thousand (total value – 587.8 million lats) and FOP was 19.2 thousand. The daily average of financial instruments transfers processed via DENOS stood at 170 and DVP value was 2.4 million lats. DENOS ensured 99.3% availability.

To promote integration of Latvia's payment systems into SEPA, Latvijas Banka continued its involvement in the SEPA Project in 2013 by steering the NSWG, taking part in the SEPA Working Group of the Payment Committee of the ACBL and EU Forum of the National SEPA Coordination Committees organised by the EC.

In 2013, the oversight of Latvia's payment systems was conducted in accordance with "The Payment and Securities Settlement System Policy of Latvijas Banka" (approved by the Council of Latvijas Banka Resolution No. 189/6 of 13 January 2011). The oversight policy of the ECB became binding on Latvijas Banka upon the euro changeover and

joining of the Eurosystem, hence Latvijas Banka revoked "The Payment and Securities Settlement System Policy of Latvijas Banka" as of 1 January 2014. Latvijas Banka performs the oversight of payment and securities settlement systems as of 1 January 2014 in accordance with the oversight policy stipulated by the ECB for payment systems.

## **1. OVERSIGHT OF SYSTEMICALLY IMPORTANT PAYMENT AND SECURITIES SETTLEMENT SYSTEMS**

**In 2013, Latvijas Banka pursued activities to prepare for the introduction of the euro in Latvia and successful changeover of Latvijas Banka payment systems from the settlement in lats to the settlement in euro. Latvijas Banka performed data simulations of the SAMS and TARGET2-Latvija to assess liquidity adequacy in TARGET2-Latvija after the changeover to the euro and concluded that a sufficiently high level of liquidity will be provided in TARGET2-Latvija for a complete execution of all payments submitted by the system's participants.**

**Latvijas Banka performed a compliance assessment of DENOS against the Eurosystem User Standards in cooperation with the Eurosystem to enable the use of DENOS and Latvia's securities registered with DENOS in the Eurosystem's monetary policy operations as of the changeover to the euro. DENOS was deemed to be eligible for the use in the Eurosystem's monetary policy operations and intraday credit operations as of 1 January 2014.**

**In 2013, Latvijas Banka, in the capacity of an overseer of the systemically important payment and securities settlement systems, performed a day-to-day oversight and assessed systemic risk.**

In 2013, Latvijas Banka pursued activities to prepare for the introduction of the euro in Latvia and successful changeover of Latvijas Banka payment systems from the settlement in lats to the settlement in euro. Latvijas Banka performed data simulations of TARGET2-Latvija to assess both the adequacy of liquidity in TARGET2-Latvija after the changeover to the euro and the scope of impact on the participants' settlements, should any of its three largest participants default on payments. Subject to preliminary estimates (at the time of making simulations), the Eurosystem's minimum reserve ratio might be up five times lower as of 1 January 2014 than the lats minimum reserve ratio until the euro changeover, hence it was assumed that the value of funds on TARGET2-Latvija participants' settlement accounts would be lower than on the SAMS accounts. The data of TARGET2-Latvija were simulated in order to establish whether the new level of liquidity would not cause delay in the execution of the participants' payments in TARGET2-Latvija since also the payments previously made in lats via the SAMS would be processed in TARGET2-Latvija after the changeover to the euro. Latvijas Banka carried out the simulation with caution, assuming that funds balance of TARGET2-Latvija participants after 1 January 2014 would be consistent with the projected minimum reserve ratio of the Eurosystem plus excess reserves maintained by the SAMS. It was concluded upon assessing liquidity adequacy in TARGET2-Latvija that despite a lower projected level of liquidity on the participants' settlement accounts with TARGET2-Latvija, a sufficient level of liquidity would be provided in TARGET2-Latvija to settle all payments of TARGET2-Latvija participants.

Latvijas Banka, in cooperation with the Eurosystem, performed the compliance assessment of DENOS against the ECB *Standards for the Use of EU Securities Settlement Systems in Credit Operations of the European System of Central Banks* (the

Eurosystem User Standards)<sup>2</sup> in 2013 to enable the use of Latvia's securities registered with the LCD in the Eurosystem monetary policy operations and use of DENOS for the settlement of the Eurosystem credit operations as of the changeover to the euro. The objective of the Eurosystem User Standards is to enable the execution of the Eurosystem credit operations via those securities settlement systems which do not pose any additional risk to the national central banks of the euro area countries in conducting monetary policy operations and granting intraday credits to TARGET2 participants.

DENOS was deemed to be eligible for the use in the Eurosystem's monetary policy operations and intraday credit operations as of 1 January 2014. On 1 January 2014, DENOS was included in the list of eligible securities settlement systems published by the ECB.

Latvijas Banka provided consultations to the LCD to ensure smooth transition of DENOS to the euro in TARGET2-Latvija. The LCD joined TARGET2-Latvija on a timely basis, prior to that completing the relevant tests and adapting DENOS regulations for the settlement in euro.

## 1.1 The SAMS

**In 2013, the SAMS was the only systemically important payment system for the settlement in lats in Latvia. According to statistical data, the total volume of payments processed via the SAMS recorded a year-on-year growth of 2.3% in 2013, totalling 235.0 thousand per annum, while the total value of payments increased by 13.0% and totalled 125.6 billion lats per annum. The daily average of payments processed via the SAMS accounted for 936 payments with the value of 500.5 million lats. The SAMS availability was 100.0% in 2013. The analysis of systemic risk suggested that risk still remained low. The operation of the SAMS has been terminated along with the changeover to the euro (on 1 January 2014).**

Latvijas Banka converted the SAMS participant settlement account balances in lats into the euro and terminated the operation of the SAMS as of the changeover to the euro.

To proceed with the evaluation of liquidity conditions in the system and notice any potential signs of operational risk on a timely basis, Latvijas Banka performed a day-to-day or ongoing oversight in 2013, focussing on the assessment of both the system's availability and incidents and analysing their impact on other systems, and performing analysis of the SAMS statistical data.

### Analysis of the system's statistical data

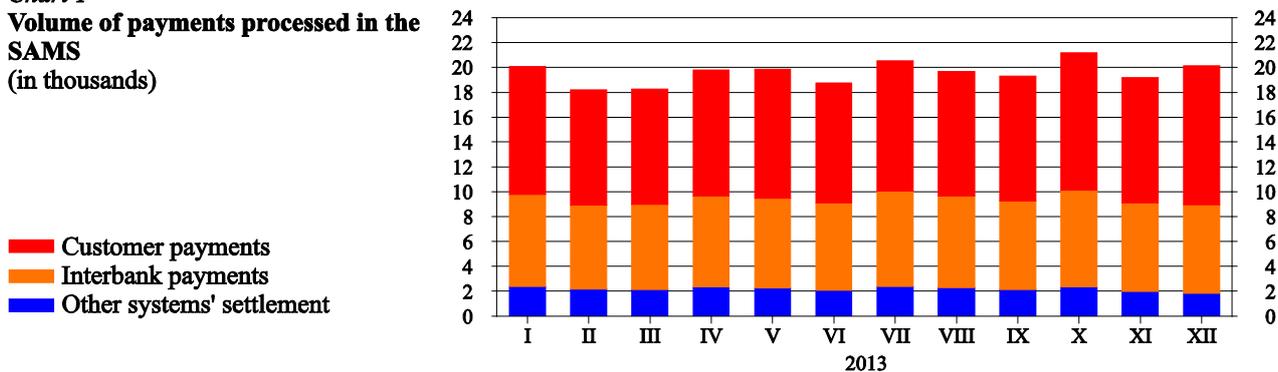
At a monthly frequency, Latvijas Banka compiled detailed information on the payments executed via the SAMS over the previous month. Statistical data were published on the website of Latvijas Banka as well as used for compiling the reports of Latvijas Banka.

<sup>2</sup> The ECB performs the assessments against the Eurosystem User Standards in line with the Eurosystem's methodology, the national central bank acts in the capacity of the first assessor monitoring the operation of a system, one of the central banks of the Eurosystem acts in the capacity of the second assessor, and other central banks of the Eurosystem may provide comments regarding the assessment. The Legal Committee of the ECB is involved in the assessment of legal framework. The Governing Council of the ECB approves the results of an assessment.

At the end of 2013, 25 credit institutions (including five branches, registered in Latvia, of credit institutions registered in other countries and one foreign credit institution), the Treasury and Latvijas Banka were the participants in the SAMS until the termination of the SAMS operation (one participant less than at the end of 2012). In March 2013, *Lietuvos bankas* commenced participation in the system, albeit on 15 November *Lietuvos bankas* decided to terminate its participation therein. JSC GE Money Bank also terminated its participation in the system. In 2013, the volume of payments processed in the SAMS recorded a year-on-year increase of 2.3%, totalling 235.0 thousand, and the total value of payments rose by 13.0% (to 125.6 billion lats; see Charts 1 and 2).

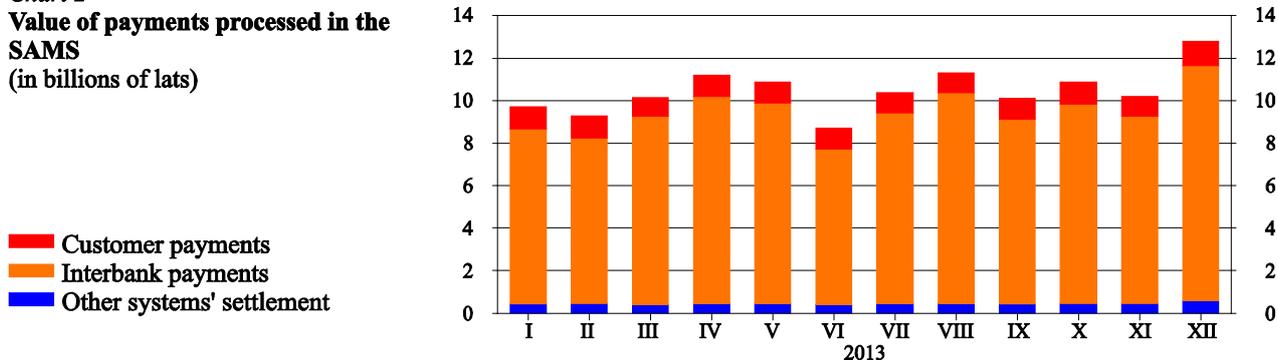
**Chart 1**

**Volume of payments processed in the SAMS**  
(in thousands)



**Chart 2**

**Value of payments processed in the SAMS**  
(in billions of lats)



In 2013, the share of interbank payment value reached 86.1% in the SAMS, that of customer payment value was 9.5% and share of interbank and customer payment volume accounted for 36.9% and 51.9% respectively. Final settlement of ancillary systems accounted for other payments, with their share reaching 4.3% and 11.2% in the SAMS in terms of the value and volume respectively.

Final settlement of the following card payment systems: *MasterCard Europe Sprl* and *Visa Europe Services Inc.* and *First Data Latvia Ltd* as well as that of the *EKS* and *DENOS* was provided through SAMS in 2013.

The availability of the SAMS was 100.0% over the reporting period, unchanged from 2012. The developments associated with the maintenance of the system's operation did not lead to operational failures.

**Risk assessment**

In 2013, the SAMS was the only systemically important payment system for the lats settlements in Latvia, since it continued to provide real-time gross settlements in lats for the monetary policy operations of Latvijas Banka, large-value interbank payments, final

settlement or netting of other payment systems operating in Latvia and urgent customer payments.

Three indicators were analysed to assess systemic risk, overall pointing to the probability of the materialisation of systemic risk: 1) the share of the system in the respective segment of payments; 2) concentration ratio and 3) netting effect ratio. The share of a systemically important payment system in the respective segment of payments exceeding 80% and at the same time a concentration ratio exceeding 80% point to a systemic risk, where the netting effect ratio is above 100%.

In 2013, 94.1% of all interbank credit transfers initiated in Latvia in lats were effected through the SAMS and their share of value accounted for 95.2% (94.3% and 92.0% respectively in 2012). The volume concentration ratio of the SAMS was 72.2% and value concentration ratio stood at 78.5% in 2013 (69.9% and 76.8% respectively in 2012).

The netting effect ratio of the SAMS describing the use of settlement funds in the case of a gross settlement system was 27.0% in 2013 (30.7% in 2012). It was calculated as the ratio of the annual average value of daily payments sent by the participants via the SAMS to the average daily balance on the participants' accounts with Latvijas Banka. In 2013, the above accounted for 315.6 million lats and 1.2 billion lats respectively<sup>3</sup>. The netting effect ratio remained low. The value of payments executed per day in efficient payment systems may even several times exceed that of the funds available on the accounts. Such a netting effect ratio may be attributed to the fact that deposits held by credit institutions in lats settlement accounts with Latvijas Banka are used both for making payments and fulfilling the minimum reserve requirements stipulated by Latvijas Banka. Hence the value of funds on settlement accounts exceeds the value required for the payment execution. The share of SAMS in the respective segment of payments still suggested that its systemic importance was very high in the segment of large-value interbank payments, and thus the SAMS was actually not substitutable. This means that the SAMS may exert substantial impact on the public finance system, should a default by a participant or several participants in the SAMS cause the domino effect and operation of the SAMS would be disrupted. However, concentration ratios stood below 80% and also the netting effect ratio was low (27.0%), overall pointing to a persistently low probability of systemic risk.

## 1.2 TARGET2-Latvija

**In 2013, TARGET2 was one of the systemically important payment systems in the EU. The Eurosystem conducted the oversight of TARGET2. Latvijas Banka was involved in the oversight of TARGET2 in the capacity of an observer and provided the relevant data on the operation of TARGET2-Latvija for oversight purposes. In 2013, the total volume of payments effected through TARGET2-Latvija recorded a year-on-year growth of 6.6%, totalling 349.8 thousand per annum, while the total value of payments declined by 29.0% and totalled 132.0 billion euro per annum (see Chart 3). The daily average volume of payments processed in TARGET2-Latvija was 1 372 with the value of 517.5 million euro or 363.7 million lats.**

In 2013, Latvijas Banka, along with other participants of the ESCB, provided for the operation of TARGET2 by maintaining TARGET2-Latvija, a component system of

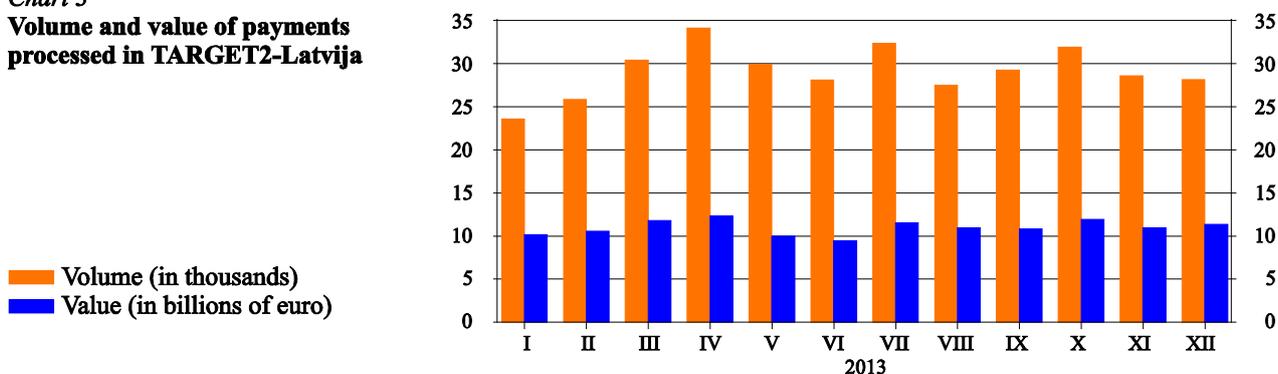
<sup>3</sup> Payments sent by Latvijas Banka are not taken into account in the calculation.

TARGET2. The Eurosystem performed an oversight of TARGET2 by conducting risk analysis and implementing the necessary risk mitigation measures. Latvijas Banka was involved in the oversight of TARGET2 in the capacity of an observer and provided the relevant data on the operation of TARGET2-Latvija for oversight purposes. At the end of 2013 there were 25 direct participants in TARGET2-Latvija (one participant less than at the end of 2012) since the Latvian Branch of *Svenska Handelsbanken AB* joined the system, whereas the JSC GE Money Bank and JSC UniCredit Bank terminated their participation in the system. 23 credit institutions (including four branches, registered in Latvia, of credit institutions registered in other countries), the Treasury and Latvijas Banka were the participants in the system. TARGET2-Latvija provided for the execution of final settlement in euro for one ancillary system, the EKS, in 2013.

The role of TARGET2-Latvija in interbank settlement remained insignificant in Latvia in 2013. Of interbank credit transfers executed in euro, the volume of interbank payments effected through TARGET2-Latvija accounted for 15.4% (19.1 thousand payments) and their value stood at 29.8% (97.4 billion euro) in 2013 (12.7% and 36.7% respectively in 2012).

In 2013, the total volume of payments processed in TARGET2-Latvija recorded a year-on-year growth of 6.6%, totalling 349.8 thousand per annum, while the total value of payments shrank by 29.0% and totalled 132.0 billion euro per annum (see Chart 3). The declining value is mainly attributable to a fall in the value of cross-border interbank payments executed by credit institutions in comparison with 2012.

**Chart 3**  
**Volume and value of payments processed in TARGET2-Latvija**



TARGET2-Latvija is a component system of TARGET2, and the system's availability ratio is calculated for the whole system. The availability ratio of TARGET2 was 100% in 2013, unchanged from 2012.

### 1.3 DENOS

In 2013, DENOS was the only systemically important securities settlement system in Latvia. According to statistical data, the volume of financial instruments transfers processed in DENOS (hereinafter under Section 1.3 DENOS, transfers) stood at 42.7 thousand in 2013 (a year-on-year decline of 15.1%), of which DVP accounted for 23.5 thousand and FOP recorded 19.2 thousand. The total value of DVP was 587.8 million lats per annum, representing a 16.3% rise over 2012. The daily average transfers and DVP processed via DENOS stood at 170 and their value was 2.4 million lats in 2013. The availability of DENOS was 99.3%. The analysis of systemic risk suggested that risk still remained low.

In 2013, Latvijas Banka identified the progress made by the LCD in implementing the recommendations issued by Latvijas Banka conducting the assessment of DENOS on compliance with the ESCB-CESR Recommendations for Securities Settlement Systems in 2012. The LCD had complied with one of the four recommendations. The LCD induced changes in the settlement procedures of DENOS to ensure the separation of settlement from the settlement of ancillary services provided by the LCD and to prevent holding overnight deposits with the LCD settlement account, thus mitigating credit and liquidity risks in line with the ESCB-CESR Recommendation No. 6 "Central Securities Depositories (CSDs)". The LCD will implement the remaining three recommendations in preparation for joining T2S from 2014 to 2017.

In 2013, Latvijas Banka assessed amendments to the LCD regulations regarding the financial instruments transfers in case of handover of the credit institution's business, and proposed to supplement draft amendments with a provision about the moment of entry of a transfer order into the system.

To assess the liquidity conditions in DENOS and notice any potential signs of operational risk on a timely basis, Latvijas Banka analysed the statistical data of DENOS and performed the incident evaluation of DENOS by examining their impact on payment systems in 2013.

#### **Analysis of the system's statistical data**

The LCD continued to provide DVP gross and net settlement for financial instruments transactions executed at the Stock Exchange as well as DVP and FOP gross settlements for financial instruments OTC transactions through DENOS.

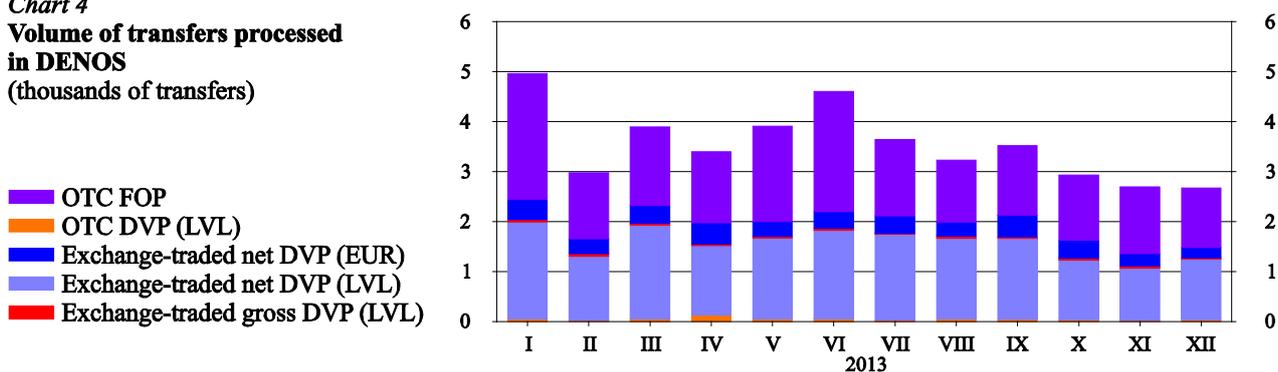
At the end of 2013, the number of DENOS participants stood at 21. The number of participants declined by one participant year-on-year, since the JSC *Latvijas Krājbanka*, JSC GE Money Bank and SJSC *Latvijas Hipotēku un zemes banka* terminated their participation in the system, albeit JSC IBS Renesource Capital and Latvian Branch of *Danske Bank AS* commenced participation in the system.

In 2013, the LCD continued to provide via DENOS the bilateral cross-border gross DVP and FOP settlements of financial instruments through the links to the Estonian CSD *Eesti Väärtpaberikeskus AS* and Lithuanian CSD *Vertybinių popierių atsiskaitymo sistema* and unilateral DVP and FOP settlements through the link to the international CSD *Clearstream Banking SA Luxembourg*, enabling the transfer of financial instruments registered with the CSD *Clearstream Banking SA Luxembourg* to the LCD. Transfers were not executed through the unilateral link of the LCD to Poland's CSD *Krajowy Depozyt Papierów Wartościowych S.A.*

The LCD continued to provide DVP settlement in lats, euro and US dollars for its participants. DVP settlement was not executed in Russian rubles in 2013. In 2013, the volume of transfers via DENOS declined by 15.1% year-on-year and totalled 42.7 thousand transfers per annum. Of the total transfer volume, 19.2 thousand (44.9%) were FOP transfers, while the remaining transfers were DVP transfers. Of all DVP transfers, 82.1% (19.3 thousand) were transfers executed in lats and 17.2% (4.0 thousand) were those made in euro (see Chart 4). The volume of DVP transfers executed in other foreign currencies was insignificant. The declining transfer volume was primarily attributable to a decrease in the volume of FOP transfers since transfers were not executed from JSC *Latvijas Krājbanka* in 2013 due to the fact that the provision of its financial services had been suspended and operation had resulted in a substantial

increase in the volume of FOP transfers in 2012. In 2013, the volume of transfers was also affected by the amendments to the LCD regulations providing for a transfer of all customer financial instruments with the same ISIN Code in a single transfer in the cases stipulated by the laws and regulations, as proposed by the *SJSC Latvijas Hipotēku un zemes banka*. In the absence of such amendments securities held by each customer would have to be transferred on a transfer-by-transfer basis and volume of the relevant transfers would have increased.

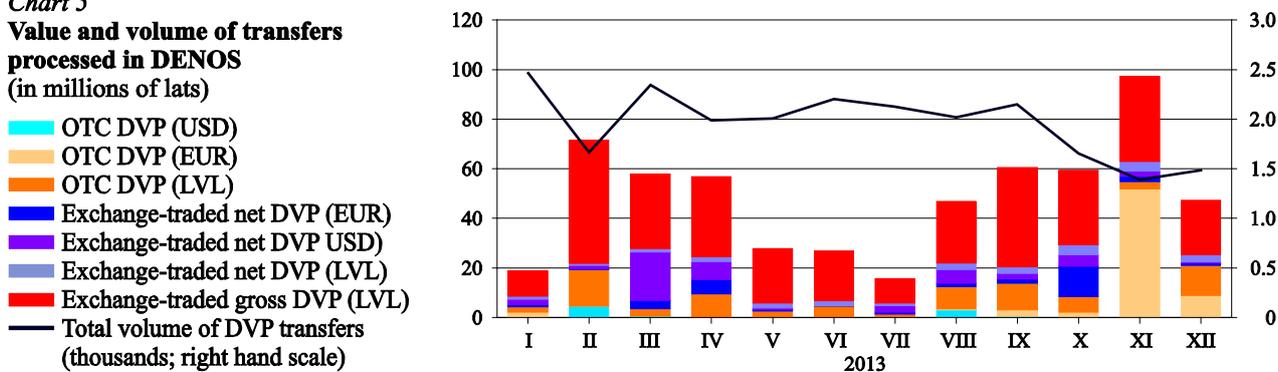
**Chart 4**  
**Volume of transfers processed in DENOS**  
 (thousands of transfers)



In 2013, the value of DVP transfers via DENOS rose by 16.3% year-on-year, totalling 587.8 million lats per annum (including the transfer value of transactions executed at the Stock Exchange – 430.9 million lats or 73.3%; see Chart 5). Of the total value of DVP transfers, 73.0% were made in lats accounting primarily for transfers of gross transactions executed at the Stock Exchange.

Higher value of DVP transfers was primarily attributable to increasing gross DVP transfers of transactions executed at the Stock Exchange associated with a growing value of transactions of the government debt securities' auctions. The central government domestic borrowing management policy and higher liquidity of credit institutions have contributed to such an increase. At the same time, a fall in the volume of DVP transfers was observed along with the rising value of DVP transfers in February and November 2013, indicating that some sizable transactions accounted for higher value rather than an increase in overall trading activity.

**Chart 5**  
**Value and volume of transfers processed in DENOS**  
 (in millions of lats)



The LCD notified Latvijas Banka via Latvijas Banka file exchange service of the operational problems incurred by DENOS or its maintenance resources and the solution thereof. Latvijas Banka monitored the problem-solving process and assessed the impact of each incident on the SAMS and its ancillary systems as well as Latvijas Banka monetary policy operations and intraday credit operations. In 2013, the availability of DENOS was 99.3% (99.6% in 2012).

## Risk assessment

In 2013, DENOS was the only systemically important securities settlement system in Latvia. Financial instruments related settlements via DENOS in lats were executed in the SAMS. DENOS was used for the monetary policy operations of Latvijas Banka and mobilisation of collateral securities of the participants in the monetary policy operations for the purpose of receiving an intraday credit in the SAMS.

In the securities settlement systems, settlement risks may be related both to cash leg settlement and financial instruments settlement. Latvijas Banka assessed the probability of the materialisation of systemic risk regarding the lats transfers via DENOS since their cash leg settlement was executed in the SAMS and could affect the operation of the SAMS which was a systemically important payment system in Latvia and ensured the settlement of monetary and intraday credit operations of Latvijas Banka in lats.

### *a) Cash leg settlement*

Two indicators were analysed over the reporting period to assess systemic risk for cash leg settlements in DENOS, overall pointing to the probability of systemic risk materialisation: 1) concentration ratio; 2) the share of payment value of DENOS in the SAMS. The concentration ratio above 80% points to the materialisation of systemic risk, if the value of DENOS cash leg settlements executed in the SAMS is substantial.

In 2013, the annual concentration ratio of DVP transfers (total gross and net) executed in lats and processed in DENOS stood at 90.3% and 88.8% in terms of the transfer volume and value (86.3% and 84.3% respectively in 2012). High concentration ratios are typical for DENOS since the securities market is smaller in Latvia than in other EU countries, thus some major players in the market are more active due to the fact that they have developed a segment of competitive securities transaction service or are more actively involved in the securities market on their own behalf.

In 2013, the value of DVP transfers executed in lats and processed via DENOS (unchanged from 2012) accounted for only 0.3% of the total value of payments processed in the SAMS. In 2013, the daily average balance on the SAMS accounts was 1.2 billion lats, 315 million lats were on average used for credit institution cash settlement per day, while the daily average value of settlement executed by DENOS via the SAMS accounted for 1.7 million lats. The value of DENOS cash leg settlement executed in the SAMS was minor; hence the operation of the SAMS was not impaired.

In 2013, the concentration ratios of DENOS were above 80% while the value of DENOS cash leg settlement executed in the SAMS was minor, overall pointing to low probability of the systemic risk materialisation.

### *b) Financial instruments settlement*

Systemic risk to securities settlement systems may arise if a seller of financial instruments fails to provide financial instruments for the buyer on the settlement day, whereas the buyer needs these instruments for a further discharge of obligations. The value of outstanding transfers was analysed to assess systemic risk for financial instruments settlement in DENOS. As stipulated in the ESCB-CESR Recommendations, outstanding transfers entail substantial additional risk, if the value of outstanding transfers exceeds 5% of the total value of transfers executed in a securities settlement system.

According to the data reported by the LCD, in 2013 more than 99.99% of transfers were settled in DENOS on the intended settlement date in terms of the volume and value respectively (the same as in the previous year), while, out of transfers outstanding on the settlement date, 99.99% were settled within one or two business days of the outstanding transfer date. The value of outstanding transfers is below 5% in DENOS, hence it can be concluded that this ratio points to a low probability of the materialisation of risk.

The analysis of systemic risk suggested that the materialisation of systemic risk was persistently low in DENOS in 2013 overall.

## 2. RETAIL PAYMENT SYSTEMS

**To prepare for the changeover to the euro in a timely manner and make sure that the EKS was ready for this changeover, Latvijas Banka performed an assessment of the EKS compliance with the Core Principles. Latvijas Banka in its evaluation acknowledged that the EKS was fully in line with all applicable Core Principles.**

**Latvijas Banka carried out work in due time to prepare the EKS for the euro changeover, assessing the introduction of additional clearing cycles from the oversight perspective. The additional cycles provided efficient settlement of payments in euro in a timely manner. These cycles also ensured more frequent execution and receipt of cross-border payments in euro. As of the introduction of the euro in Latvia on 1 January 2014, the EKS provides only processing of SEPA credit transfers in euro.**

To prepare for the introduction of the euro in a timely manner and make sure that the EKS is ready for the transition from processing payments in lats to processing them in euro, Latvijas Banka performed an assessment of the EKS compliance with the Core Principles at the beginning of the year. At the time of the assessment (since the last EKS assessment in 2011), significant changes had not taken place in the functionality of the system and its governing legislative documents which might impact the compliance of the EKS with the Core Principles. Processing of payments in lats via the EKS was terminated after Latvia joined the euro area; the functionality of processing payments in euro and the legal framework were retained. Therefore, when evaluating the EKS, its legal framework and functionality were assessed only with regard to settlement in euro. Latvijas Banka acknowledged that the EKS complied with all applicable Core Principles. Given the volume of payments processed through the EKS, the system was qualified as a systemically prominent payment system. Consequently, the EKS evaluation has to be carried out in accordance with the Eurosystem practice by involving the ECB and a Eurosystem central bank only after the introduction of the euro (in 2014 or 2015).

On 3 January 2013, Latvijas Banka performed a repeated self-assessment of the EKS SEPA in line with the SEPA compliance provisions developed by the ECB. The self-assessment confirmed the compliance of the EKS with the SEPA requirements and the SEPA Credit Transfer Rulebook updated by the European Payments Council. The EKS self-assessment has been published on the websites of Latvijas Banka and SEPA Latvia.

In 2013, Latvijas Banka introduced additional settlement cycles in the EKS to reduce risks in the EKS cross-border settlement, especially taking into consideration the fact that several significant participants (JSC *Swedbank*, JSC *SEB banka*, the Latvian Branch of *Nordea Bank Finland Plc*, the Latvian Branch of JSC *Danske Bank*, the Latvian Branch of *Svenska Handelsbanken AB*, the Latvian Branch of *Pohjola Bank plc*) decided

to terminate their participation in the EKS after the introduction of the euro, and that in 2014 a large part of domestic payments in the EKS will be executed as cross-border payments in euro via other EU payment systems.

In 2013, Latvijas Banka advised *Latvijas Pasts* on the necessary actions to be taken to prepare the PNS for the changeover to the euro and to ensure efficient migration to SEPA credit transfers as of 1 January 2014. At the end of the year, Latvijas Banka organised a survey on the readiness to migrate to SEPA credit transfers. In the survey, *Latvijas Pasts* confirmed its readiness to replace all lats payments in the PNS with SEPA credit transfers in euro as of 1 January 2014.

In response to the notification that JSC *OpusCapita* (JSC *Itella Information* until 1 November 2013) will not convert the automatic payment system into a SEPA direct debit payment infrastructure and will not offer SEPA direct debit payments, Latvijas Banka organised a discussion among JSC *OpusCapita*, credit institutions and enterprises to ensure the transition of the automatic payment system to the euro as of 1 January 2014 and to agree on the solution meeting SEPA requirements to be used for the replacement of national direct debit payments. Pursuant to Regulation (EU) No. 260/2012 of the European Parliament and of the Council of 14 March 2012 establishing technical and business requirements for credit transfers and direct debits in euro and amending Regulation (EC) No. 924/2009 (hereinafter – the SEPA Regulation), the national direct debit payments must be replaced by the respective SEPA products from 1 January 2015. As a result of the discussions organised by Latvijas Banka, market participants decided to agree by 1 January 2014 on the most efficient solution to be employed for the replacement of the national direct debit payments by 1 January 2015. At the end of the year, Latvijas Banka advised JSC *OpusCapita* credit institutions and enterprises on the proposal of JSC *OpusCapita* to replace the national direct debit payments by SEPA credit transfers combined with e-invoicing.

## 2.1 The EKS

**In 2013, the EKS was a systemically prominent retail payment system. In 2013, the volume of payments executed in lats and processed in the EKS increased by 0.4% year-on-year, reaching 33.7 million payments, while the total value rose by 1.7% amounting to 12.4 billion lats (134.1 thousand payments totalling 49.2 million lats on average per day). In 2013, the volume of payments executed in euro and processed in the EKS swelled by 27.9% year-on-year, reaching 900.3 thousand payments per year, while the total value augmented by 35.2% adding up to 8.4 billion euro per annum (3.5 thousand payments equalling 32.8 million euro or 23.1 million lats on average per day). Of all customer credit transfers executed among credit institutions in Latvia in lats, 71.3% and 71.1% were processed in lats via the EKS in terms of volume and value respectively. The EKS availability ratio stood at 99.83%. The systemic risk analysis pointed to minimal probability of systemic risk.**

To enable payment institutions to integrate into the SEPA by offering customers services of SEPA credit transfers, Latvijas Banka decided to introduce the status of the addressable BIC holder into the EKS. This system functionality was successfully introduced in June 2013.

In 2013, the EKS was used for processing retail payments in lats and euro. The EKS continued to ensure fully automated payment processing; it accepted and processed only electronic payment documents. The EKS final settlement in lats was effected in the participants' accounts opened with Latvijas Banka in the SAMS, while that in euro was executed in the participants' accounts opened with Latvijas Banka in TARGET2-Latvija.

In order to note the signs of operational risk in advance, a day-to-day or ongoing oversight of the EKS was performed in 2013 by collecting and analysing the system's statistical data and by observing its operation.

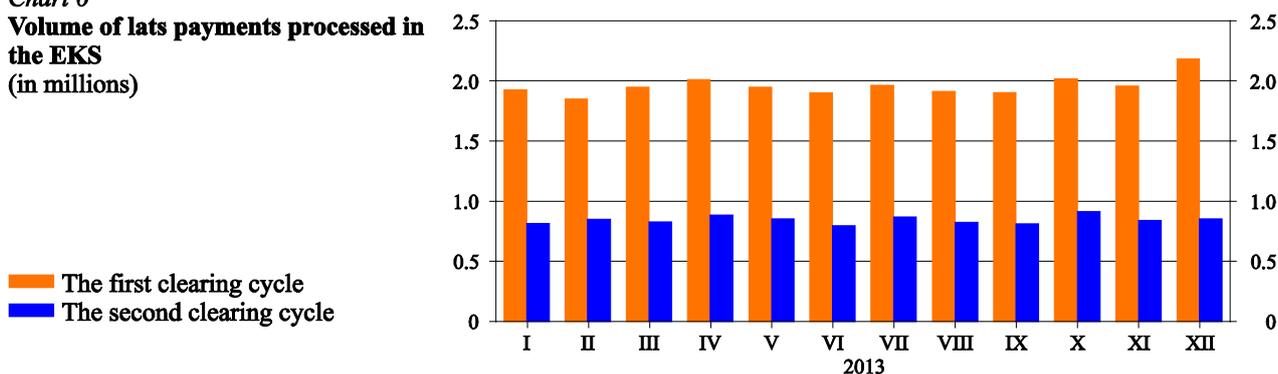
**Analysis of the system's statistical data**

At the beginning of each month of 2013 (similar to the SAMS), Latvijas Banka compiled information on the payments executed via the EKS in the previous month. Data were published on the website of Latvijas Banka on a monthly basis, and the detailed information was employed for compiling reports of Latvijas Banka.

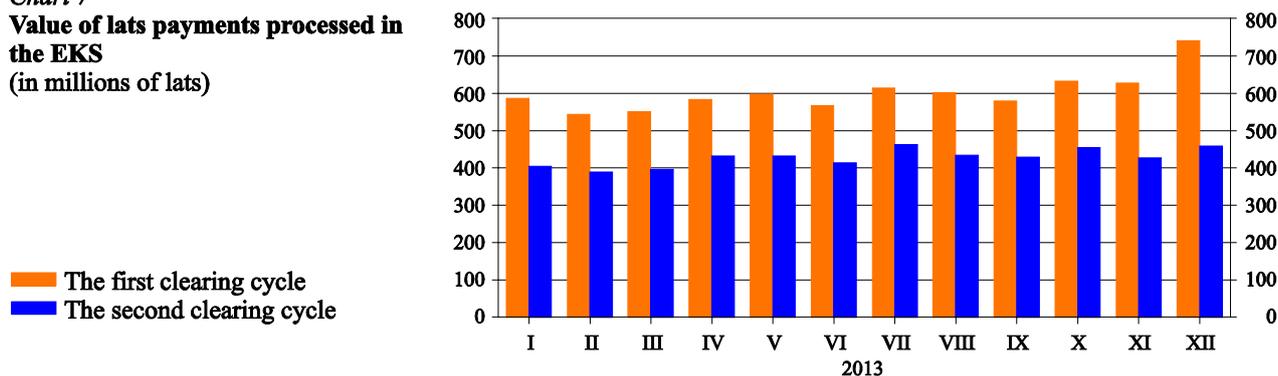
At the end of 2013 (until the termination of lats payments made via the EKS), 23 credit institutions (including five branches, registered in Latvia, of credit institutions registered in other countries), the Treasury and Latvijas Banka participated in lats settlement via the EKS. *Latvijas Pasts* joined the EKS as an indirect participant for lats payments, but *JSC GE Money Bank* and *JSC UniCredit Bank* terminated their participation in the system. 16 credit institutions (including one branch, registered in Latvia, of a credit institution registered in another country), the Treasury and Latvijas Banka took part in the EKS euro settlement. *JSC SMP Bank* commenced participation in the EKS system for settlement in euro, while *JSC GE Money Bank* and *JSC UniCredit Bank* terminated their participation in it.

In 2013, the volume of payments executed in lats and processed in the EKS increased by 0.4% year-on-year, totalling 33.7 million per annum, while their value rose by 1.7%, reaching 12.4 billion lats per annum. The average value per payment made in 2013 expanded to 367.08 lats (362.40 lats in 2012). Of all lats payments submitted and processed daily in the EKS, 69.9% and 58.4% in terms of volume and value respectively were processed in the first clearing cycle (from 8.30 to 10.30; see Charts 6 and 7).

**Chart 6**  
**Volume of lats payments processed in the EKS (in millions)**

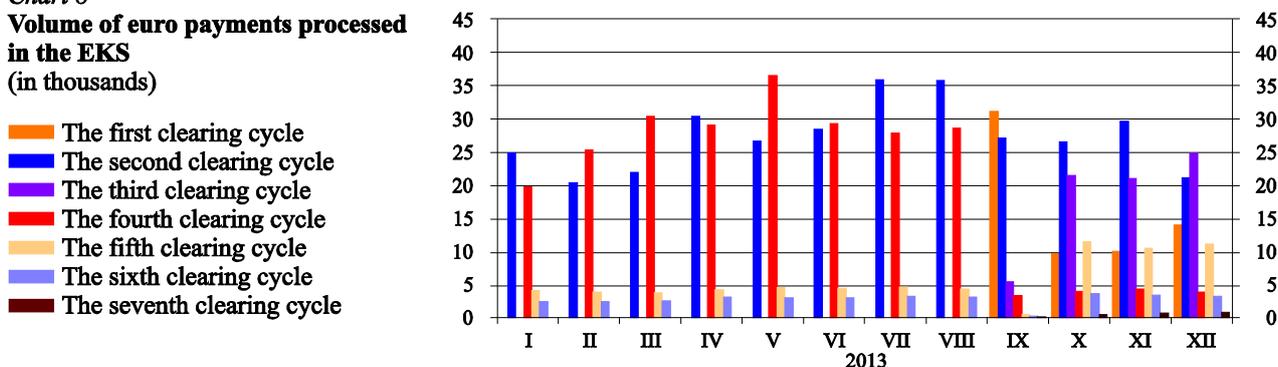


**Chart 7**  
**Value of lats payments processed in the EKS (in millions of lats)**

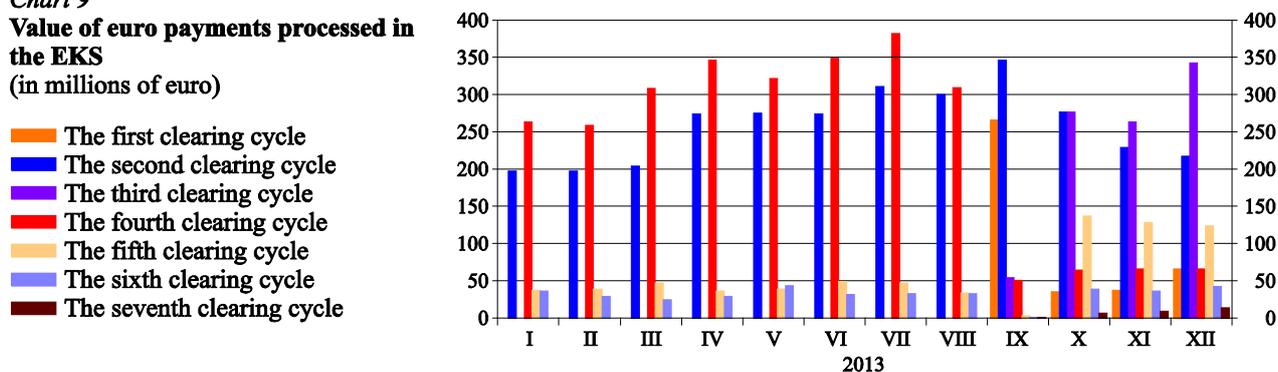


In 2013, the total volume of euro payments processed via the EKS increased by 27.9% (to 900.3 thousand) year-on-year, while the total value expanded by 35.2%, reaching 8.4 billion euro (see Charts 8 and 9). Since the transformation of the EKS (in 2010) into a payment system meeting the SEPA requirements, a steady and sharp growth in the volume and value of the euro payments processed annually in the EKS has occurred among almost all its participants. In 2013, the average value per payment executed via the EKS in euro stood at 9 301 euro (8 802 euro in 2012). In preparation for the euro changeover and ensuring efficient settlement of euro payments in advance, including those submitted to the credit institutions registered in Latvia which do not participate in the EKS for settlement in euro, Latvijas Banka increased the number of clearing cycles for euro settlement via the EKS from four to seven per day on 30 September 2013. These additional cycles also guaranteed more frequent execution and receipt of cross-border payments in euro.

**Chart 8**  
**Volume of euro payments processed in the EKS**  
 (in thousands)



**Chart 9**  
**Value of euro payments processed in the EKS**  
 (in millions of euro)



On the basis of the information entered into the Incident Register, overseers were promptly notified of the operational problems incurred by the EKS or its maintenance resources and the solution thereof, and they monitored the problem-solving process accordingly.

The EKS availability ratio stood at 99.83%, i.e. such a share of the entire EKS net position or offsetting settlement was executed within the stipulated time frame. Overall, three times out of 1 715 the delays in settlement exceeded 30 minutes of the clearing cycle time in 2013. All clearing delays in the EKS were due to settlement in euro.

In cases of EKS critical incidents (the incidents which caused delays in settlement exceeding 30 minutes of the clearing cycle time) Latvijas Banka assessed the impact of the specific incident on other payment systems and established that the EKS critical incidents in 2013 did not adversely affect other payment systems and participants'

liquidity; Latvijas Banka did not find default either as disruptions were eliminated in a timely manner and settlement in the EKS was completed. Latvijas Banka made the necessary changes in the EKS and processes to reduce, to the fullest extent possible, the recurrence of similar incidents in the future.

## Risk assessment

Pursuant to the ECB document *Oversight Standards for Euro Retail Payment Systems*, the clearing and retail payment systems are deemed systemically important retail payment systems if they process more than 75% of payments executed in the relevant segment and the volume of payments executed therein exceeds 10% of the transaction value of the relevant large-value interbank payment system. In compliance with these standards, the concentration and netting effect ratios of systemically important retail payment systems are analysed, since these ratios may suggest a higher systemic risk, should both of them exceed certain limits at the same time. A concentration ratio above 80% points to systemic risk in the event that the netting effect ratio is below 10%.

The retail payment systems that do not meet the criteria of a systemically important retail payment system are deemed to be systemically prominent if they process more than 25% of payments executed in the relevant segment. In 2013, of all customer credit transfers executed among credit institutions in Latvia in lats, 71.3% and 71.1% were effected through the EKS in terms of volume and value respectively (71.7% and 73.4% in 2012 respectively). In 2013, the total value of the payments executed in lats and euro via the EKS (in the lats equivalent) amounted to 18.2 billion lats or 8.4% of the total value of payments processed in the SAMS and TARGET2-Latvija in the lats equivalent. Thus, the EKS was a systemically prominent retail payment system in 2013. However, given the relatively high importance of the EKS in the settlement of lats payments, in 2013, Latvijas Banka additionally analysed the concentration and netting effect ratios of the payments executed in lats via the EKS.

In 2013, the volume concentration ratio of the payments made in the EKS in lats increased to 84.7% and the value concentration ratio rose to 84.0% (81.4% and 81.0% in 2012 respectively).

In 2013, the netting effect ratios of the payments executed via the EKS in lats in the first and second clearing cycles (i.e. the system participants' net positions as a percentage of the system's gross transaction value) amounted to 16.6% in the first clearing cycle and 12.7% in the second clearing cycle (24.0% and 17.3% respectively in 2012). Despite the relatively high concentration ratios, the systemic risk in the EKS remained low, since the netting effect ratio exceeded 10%.

## 2.2 The FDL

**The FDL qualified as a systemically prominent retail payment system in Latvia. Within the scope of the oversight, Latvijas Banka requested the FDL to provide data on the card transactions processed in the FDL on a semi-annual basis. In 2013, the market share of the transactions conducted at terminals with credit institution cards and processed via the FDL shrank.**

Within the framework of the oversight, the overseers received data from the FDL on the volume and value of the processed card transactions, customers served, concentration and net settlement positions on a semi-annual basis. The compiled data were used to

monitor the FDL development. The FDL data were not made public subject to the confidentiality requirements.

In 2013, the FDL provided payment card authorisation and calculated the card transaction net positions in lats. In 2013, the total value of the final settlement of the FDL processed via the SAMS was lower in comparison with that of the final settlement of the card payment system *MasterCard Europe Sprl* but higher than that of the card payment system *Visa Europe Services Inc.*

As regards international transactions, some Latvian credit institutions had concluded direct agreements with international card scheme centres or they could also execute card payments through parent credit institutions or their payment card authorisation centres. Latvijas Banka analysed FDL market shares in respect of the total of Latvian credit institution transactions effected with credit institution cards at terminals; however, the data of this analysis are classified as restricted information and are not made public. The FDL market share narrowed in 2013 in comparison with 2012, albeit the FDL still maintained the status of a systemically prominent system. The majority of Latvian credit institutions used the FDL for processing local settlement. Individual credit institutions also employed FDL services for complete or incomplete processing of intrabank transactions.

The net position settlement of payments processed via the FDL was executed among credit institutions in the SAMS each business day, while payments made in Latvia with cards issued outside the country and transactions effected abroad with cards issued in Latvia were settled at international card scheme centres.

After the euro changeover on 1 January 2014, *MasterCard Europe Sprl* and *Visa Europe Services Inc.* made subsequent settlement with credit institutions by using accounts in foreign credit institutions opened specifically for this purpose. The FDL connected to TARGET2- Latvia.

## 2.3 The PNS

**Latvijas Banka compiled information on the PNS which processed 8.3 million transactions in the total value of 0.57 billion lats. The volume of PNS customer payments declined by 7.4%, and the value shrank by 8.6% year-on-year in comparison with 2012.**

In 2013, Latvijas Banka requested *Latvijas Pasts* to provide data on the payments processed via the PNS in the first and second halves of the year. Payment statistics was published on the website of Latvijas Banka. On 10 November 2000, the incorporation of PNS statistical data into the report on Latvia's payment statistics was agreed upon with *Latvijas Pasts* in writing.

In 2013, *Latvijas Pasts* continued to maintain the network of post offices and ensure the provision of payment services, offering credit transfer and direct debit services to its customers. The total volume of customer payments processed via the PNS decreased by 7.4% (to 8.3 million), and the total value contracted by 8.6% (to 0.57 billion lats) year-on-year. The average value per payment was 69.06 lats in 2013. The PNS processed 2.8% (8.3 million transactions) of the customer payments executed in Latvia, however, the value of such transactions amounted to a mere 0.14% (0.57 billion lats) of the total value of customer payments made in Latvia.

## 2.4 JSC *OpusCapita* automatic payment system

As in the previous periods, JSC *OpusCapita* was the only company providing infrastructure for interbank direct debit payments in Latvia also in 2013. The JSC *OpusCapita* automatic payment system was a systemically prominent retail payment system in 2013. Latvijas Banka gathered information on JSC *OpusCapita* and statistical data on its automatic payment system.

On 1 November 2013, JSC *Itella Information* changed its name to JSC *OpusCapita*. JSC *OpusCapita* acquired its name from a JSC *Itella Information* subsidiary which has already been specialising in offering solutions for financial processes for 29 years. The objective of these changes is to focus on the company's strength, i.e. the development of more efficient and higher quality solutions for financial processes.

The JSC *OpusCapita* automatic payment system provides diverse payment-related services, including processing of direct debit payments, enabling automatic processing of invoices regarding mutual settlement among customers, companies and credit institutions, while credit institutions execute cash settlement for automatic payments outside the JSC *OpusCapita* automatic payment system.

In 2013, within the scope of the oversight, Latvijas Banka requested JSC *OpusCapita* to provide data on the volume and value of direct debit payments processed in the first and second halves of the year, five largest participants in the system, as well as information on the number of agreements concluded with credit institutions, companies and customers. The data reported by JSC *OpusCapita* were not made public subject to the confidentiality requirements.

## 3. PAYMENT INSTRUMENTS

**In 2013, pursuant to the "Payment and Securities Settlement System Policy of Latvijas Banka", information on payment instruments used in Latvia in 2013 was compiled and analysed. In 2013, development of payment instruments was steady, and hence it was not necessary to implement risk containment measures with regard to the use of payment instruments.**

On the basis of Latvijas Banka Regulation No. 74 "Regulation for Compiling 'Credit Institution and Electronic Money Institution Payment Statistics Report'" of 12 May 2011, Latvijas Banka continued to collect statistical data on payment instruments. The overseers receive statistical data from the Treasury subject to an agreement and from *Latvijas Pasts* – subject to an arrangement, and the above data are compiled in accordance with the methodology stipulated by the "Regulation for Compiling 'Credit Institution and Electronic Money Institution Payment Statistics Report'". Latvijas Banka provided a brief analytical insight into the area of payment systems on the website.

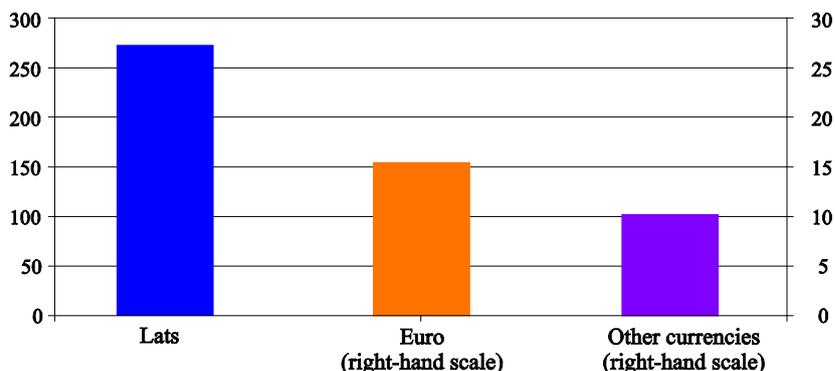
Latvijas Banka monitored development of payment cards, terminals and ATM networks by analysing the data received from credit institutions and the FDL.

### 3.1 Development of payment instruments

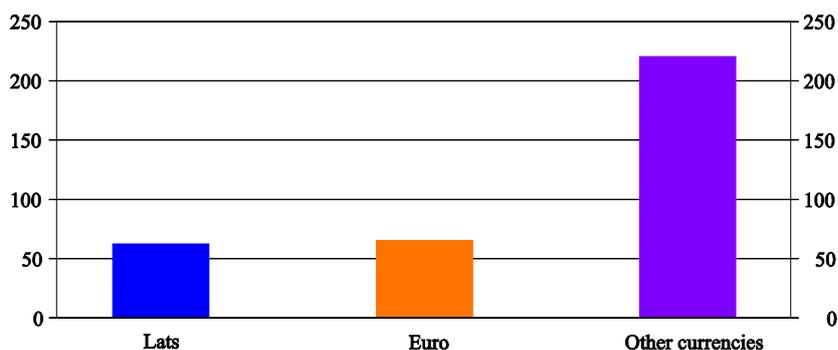
In 2013, the total volume and value of customer payment instruments used in Latvia rose by 12.8% (to 297.7 million) and 17.8% (to 407.0 billion lats) respectively. Of all customer payment instruments, the volume of payments executed in lats amounted to

91.4%, that in euro stood at 5.2% and in other currencies it was 3.4% (see Chart 10). In terms of value, the majority of payments (64.9%) were made in other currencies, 18.6% were executed in euro and 16.6% – in lats (see Chart 11).

**Chart 10**  
**Volume of payments by currency**  
**in 2013**  
**(in millions)**

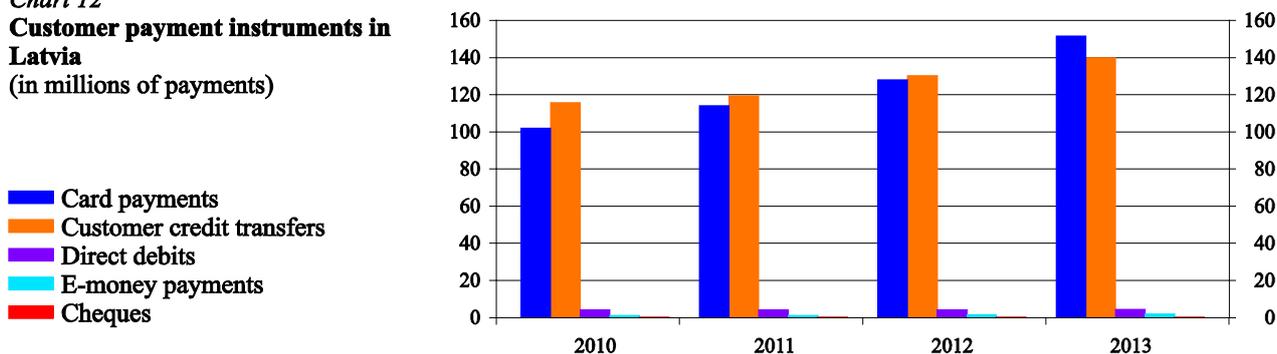


**Chart 11**  
**Value of payments by currency**  
**in 2013**  
**(in billions of lats)**



When assessing the use of individual payment instruments, it should be concluded that card payments and customer credit transfers (50.9% and 46.9% respectively) were employed most frequently out of all customer payment instruments (see Chart 12).

**Chart 12**  
**Customer payment instruments in Latvia**  
**(in millions of payments)**



The volume of payments made with payment cards issued in Latvia recorded a year-on-year increase of 18.5% (to 151.6 million), whereas their value increased by 17.6% (to 2.3 billion lats). 84.2% of their total volume was transactions undertaken at physical locations of card payments or at POS terminals in shops and other points of sale. The rest 15.8% of card payments were remote transactions executed online or by telephone. The increase in the total volume of card payments was mainly due to the surge of online and telephone payments by 96.6% (their value augmented by 69.9%). The growth of card payments at terminals was moderate in terms of volume (10.3%) and value (11.3%).

Data on the payments made at Latvian terminals with payment cards issued abroad were also compiled. In 2013, the volume of these payments was 16.1 million, while their value stood at 474.5 million lats. The volume and value of payments made at Latvian terminals with foreign payment cards rose by 56.8% and 75.8% respectively year-on-year.

The volume and value of customer credit transfers increased by 7.3% (to 139.7 million) and 17.8% (to 404.6 billion lats) respectively compared with 2012. The upward trend of the customer credit transfer value was primarily prompted by the increase in the value of customer credit transfers initiated via the internet in other currencies (23.6%).

Payments executed by credit institution customers accounted for the largest share in the total customer payments in terms of volume (92.6% or 275.8 million) and value (96.4% or 392.4 billion lats). The share of payments made by the Treasury's customers amounted to 4.6% (13.6 million) and 3.3% (13.4 billion lats) in terms of volume and value respectively, and the share of payments executed by *Latvijas Pasts* customers stood at 2.8% (8.3 million) and 0.1% (0.6 billion lats) in terms of volume and value respectively. The payments made by Latvijas Banka customers accounted for the remaining share.

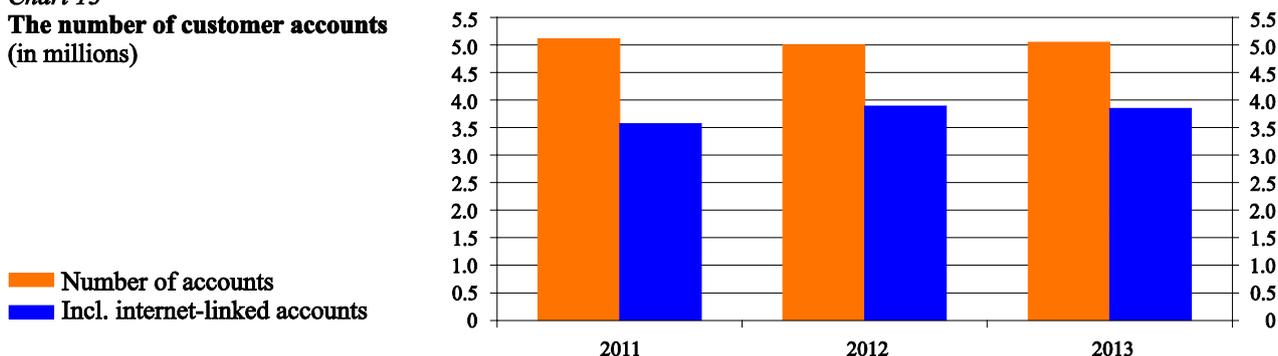
At the end of 2013, payment cards were offered by 20 credit institutions in Latvia. Overall, credit institutions had issued 2.4 million payment cards (a year-on-year increase of 17.8 thousand cards). The majority of these cards (79.2%) were issued by three credit institutions, and 84.5% of all card payments made in Latvia were executed with them. 1 177 ATMs (73.4% of which were serviced by three credit institutions), including 229 ATMs with a cash deposit function, were installed in Latvia at the end of 2013. Three credit institutions also serviced 82.9% of 25.9 thousand POS terminals.

At the end of 2013, all payment cards issued by credit institutions were those of international brands (VISA, MasterCard, American Express and others). Internationally branded payment cards were issued and serviced in line with the regulations of the respective brand card scheme, and the relevant company of international brand cards ensured compliance with them.

At the end of 2013, payment market participants had opened 5.0 million customer accounts, of which 76.2% (3.8 million) were internet-linked (see Chart 13). Three credit institutions serviced 69.2% of the total number of customer settlement accounts in Latvia.

1.9 million e-money payments totalling 24.8 million lats were also executed in 2013.

**Chart 13**  
**The number of customer accounts**  
**(in millions)**



#### 4. SEPA PROJECT

**The SEPA Project is one of the projects of Latvijas Banka devoted to the payment system oversight. In 2013, Latvijas Banka continued its involvement in the SEPA Project by steering the NSWG, taking part in the SEPA Working Group of the Payment Committee of the ACBL and EU Forum of the National SEPA Coordination Committees organised by the EC. The main goals achieved within the SEPA Project in 2013 were the approval of Version 5.0 of Latvia's National SEPA Plan and preparation for one of the most significant tasks of the SEPA implementation – ensuring changeover from the payments in lats to SEPA credit transfers in euro along with the introduction of the euro.**

As stipulated in the SEPA Regulation, SEPA credit transfers and SEPA direct debits have to be implemented in Latvia within a year following the euro changeover date. Although the SEPA Regulation stipulates that migration to SEPA credit transfers and SEPA direct debits has to be provided for by 1 January 2015, the participants in SEPA Project finalised the implementation of SEPA credit transfers earlier in Latvia, i.e. along with the changeover to the euro in Latvia. Hence, the main activities pursued within the SEPA Project in 2013 were the approval of Version 5.0 of Latvia's National SEPA Plan and preparation for one of the most significant tasks of the SEPA implementation – ensuring the changeover from the payments in lats to SEPA credit transfers in euro as of the introduction of the euro.

Credit transfers are one of the most significant payment instruments in Latvia. They account for almost half of all payments executed in Latvia. To prepare fully for the migration to SEPA credit transfers as of 1 January 2014 and replace all the relevant payments in lats, which accounted for approximately 94% of all credit transfers executed in the country in 2013, with SEPA credit transfers, the participants of Latvia's SEPA Project carried out the necessary activities in line with Latvia's National SEPA Plan and individual SEPA implementation plans. Latvijas Banka monitored the implementation of the relevant activities as well as conducted a survey whereby Latvian credit institutions, the Treasury, *Latvijas Pasts* and Latvijas Banka confirmed their readiness to replace all the relevant customer credit transfers in lats by SEPA credit transfers in euro as of 1 January 2014.

As regards SEPA communication process, Latvijas Banka carried out a number of SEPA communication activities in 2013. Latvijas Banka maintained and updated SEPA Latvia website [www.sepalatvija.lv](http://www.sepalatvija.lv), prepared a video material about SEPA "The ABC of the Economy: What is SEPA?". It was published on the website and demonstrated by Latvia's Television. At the end of the year Latvijas Banka published SEPA infographics and informational press release on SEPA, highlighting the changes in the area of payments as of 1 January 2014.

At the end of 2013, SEPA credit transfers accounted for 98.2% of all credit transfers made in euro in Latvia. 100% of ATMs, 100% of POS terminals, 99.6% of debit cards and 99.3% of credit cards were consistent with the SEPA requirements.

Reviewing Latvia's National SEPA Plan in 2013, market participants decided to reach an agreement by 1 January 2014 on an alternative solution for SEPA direct debit payments to be used for the replacement of the national direct debit payments as of 1 January 2015 since JSC *OpusCapita* took a decision that it would not develop SEPA direct debit infrastructure in Latvia.

In line with the decision of the participants of Latvia's SEPA Project to apply the derogation, stipulated in the SEPA Regulation, and waive the requirement of using XML standard until 1 February 2016, if the payment service users initiate and receive individual credit transfers and direct debit payments bundled together for transmission in the files, the ACBL has stated in Latvia's National SEPA Plan that the specifications of the national standard compliant with XML standard will be approved by the end of 2013 rather than until 1 July 2013, as has been previously planned.

The Section "SEPA Direct Debit Payments" of Latvia's National SEPA Plan was supplemented, in cooperation with the RE, with information on the subjects of the SEPA Creditor Identifier and procedure for granting the above.

The tasks performed by Latvijas Banka in the SEPA Project in 2013 have been described in Appendix.

## 5. TARGET2-SECURITIES PROJECT

**In 2013, Latvijas Banka was involved in T2S Project more actively from the perspective of the payment and securities settlement operational function of Latvijas Banka, and overseers monitored these activities. T2S Project will be completed with Latvijas Banka and the LCD joining T2S (is expected with the fourth wave of migration on 6 February 2017).**

**In 2013, T2S Feasibility Assessment regarding the readiness of Latvijas Banka to go live with T2S was completed.**

To promote integration of Latvia's securities settlement systems into the harmonised process of securities settlement of the EU Member States in euro, Latvijas Banka engaged in T2S Project in the capacity of an overseer of securities settlement systems. The settlement of securities transactions will be harmonised and cross-border settlement costs incurred by the securities market participants will be reduced as a result of implementing the above Project.

In 2013, Latvijas Banka was involved in T2S Project more actively from the perspective of the operational function of payment and securities settlement of Latvijas Banka, and overseers monitored these activities. To prepare for the participation of Latvijas Banka in T2S, in May 2013 the overseers engaged in a feasibility assessment regarding the ability to ensure interoperability of its information systems and processes with T2S platform from the aspect of functional and time frame updating. In the feasibility assessment Latvijas Banka stated that it had identified no obstacles to a successful joining of T2S. Latvijas Banka has to perform operational activities, adapt the relevant systems of Latvijas Banka as well as enter into an agreement with the network service provider to ensure successful participation in T2S.

The LCD signed T2S Framework Agreement on 26 September 2013, and the Council of Latvijas Banka approved the further steps of the project for Latvijas Banka migration to T2S.

## 6. LEGISLATIVE AMENDMENTS

In 2013, Latvijas Banka engaged in discussions and participated in drafting Latvia's position regarding the following legal proposals of the EC: Directive on payment accounts: comparability of fees, switching and access to payment accounts with basic features; Directive of the European Parliament and of the Council on payment services in the internal market and amending Directives 2002/65/EC, 2013/36/EU and 2009/110/EC and repealing Directive 2007/64/EC, and Regulation of the European Parliament and of the Council on inter-bank fees for card payments. Latvijas Banka together with the Ministry of Finance of the Republic of Latvia notified the representatives of the Latvian Merchant Association of the potential impact of the EC proposals on the area of payments.

At the beginning of 2013, Latvijas Banka, following a request of the Ministry of Finance of the Republic of Latvia, coordinated the debates among credit institutions and corporates leading to an agreement to use the derogation, stipulated in the SEPA Regulation, and until 1 February 2016 waive the requirement for the payment service providers to ensure that the payment service users who initiate or receive individual credit transfers and direct debit payments bundled together for transmission in the files use ISO 20022 XML standard. The participants agreed to notify the EC of Latvia's plans to apply the derogation stated in the SEPA Regulation.

Latvijas Banka was involved in drafting amendments to the Law "On Payment Services and Electronic Money". In July 2013, the amendments to the Law "On Payment Services and Electronic Money" were approved to ensure the compliance of Latvia's payment service providers with the requirements of the SEPA Regulation. The SEPA Regulation stipulates the requirements to apply IBAN and BIC as account identifiers and XML message standard for making payments. The SEPA Regulation provides for the reachability of the payment service providers and technical compatibility of payment systems.

In 2013, Latvijas Banka, following a request of the Ministry of Finance of the Republic of Latvia, provided comments from the oversight perspective on the compromise text of the Regulation of the European Parliament and of the Council on improving securities settlement in the European Union, central securities depositories (CSD) and amendments to Directive 98/26/EC. In 2013, the EC, the European Parliament and the Council of the EU reached a tri-party agreement on the compromise text of the above Regulation.

In 2013, Latvijas Banka continued to participate in the consultation on the ECB Regulation on payments statistics under the project of the Eurosystem. Latvijas Banka monitored the process of drafting the Regulation and all reporting requirements for the payments statistics, provided comments and submitted proposals for the draft Regulation over the consultation period. Regulation (EU) No. 1409/2013 of the European Central Bank (ECB/2013/43) on payments statistics (Payments Statistics Regulation), currently stipulating the requirements for the collection of payments statistics, was approved by the ECB on 28 November 2013. The requirements regarding the payments statistics stipulated in Guideline of the ECB of 1 August 2007 on monetary, financial institutions and markets statistics (ECB/2007/9) are replaced by the Payments Statistics Regulation. In the Payments Statistics Regulation statistical information presented previously has been supplemented with a requirement to provide data in the following breakdown: geographical (domestic, other euro area countries,

other non-euro area countries, cross-border), SEPA and non-SEPA customer credit transfers and direct debit payments, as well as supplemented with the breakdown of payments initiated electronically by type of initiation, a more detailed breakdown of e-money payment and e-money account number and breakdown by number of overnight deposits. Latvijas Banka developed draft "Regulation for Compiling 'Credit Institution, Electronic Money Institution and Payment Institution Payment Statistics Report'" to provide for compliance with the requirements of the Payments Statistics Regulation. The draft Regulation was developed on the basis of the currently effective Latvijas Banka Regulation No. 104 "Regulation for Compiling 'Credit Institution and Electronic Money Institution Payment Statistics Report'" of 16 May 2013, taking into account the requirements of the Payments Statistics Regulation regarding the reporting of payments statistics.

In 2013 Latvijas Banka was involved in the consultation on the ECB Regulation on oversight requirements for systemically important payment systems. The ECB Regulation is one of the regulatory documents for adapting the CPSS-IOSCO Principles for financial market infrastructures in the Eurosystem.

Subject to the request of the FCMC, Latvijas Banka issued opinions on draft amendments to a number of the LCD regulations in 2013.

## **7. COOPERATION WITH OTHER INSTITUTIONS**

### **7.1 Cooperation with the ECB**

In 2013, Latvijas Banka (overseers) continued to participate in the ECB working groups addressing a wide range of issues associated with the oversight of payment systems and securities market infrastructure. At the working group meetings held by the Working Group on Oversight (WGO) of the ECB Payment and Settlement Systems Committee (PSSC) and Payment Systems Policy Working Group (PSPWG), the overseers and representatives of other national central banks of the EU countries discussed the issues pertaining to the oversight of payment instruments and infrastructures and addressed the SEPA Project related matters.

The overseers together with the FCMC experts continued to participate in the European Forum on the Security of Retail Payments (SecuRe Pay), established by the ECB. In 2013, the Forum developed the Assessment guide for evaluating compliance with the "Recommendations for the Security of Internet Payments". In 2013, the overseers together with the FCMC coordinated the consultation of the European Forum on the Security of Retail Payments regarding the Recommendations for Payment Account Access Services, gave a presentation and initiated a debate at the meeting of the IT Committee of the ACBL, participated in drafting the Recommendations for the Security of Mobile Payments for the European Forum on the Security of Retail Payments, and informed market participants of the public consultation to be opened at the beginning of 2014.

The overseers took part in the ECB Securities Experts Working Group (SEWG). As regards Latvia, the euro area countries of SEWG (a standard composition) provided comments on the assessment of DENOS against the Eurosystem User Standards in 2014.

Latvijas Banka along with other national central banks of the EU countries has been reviewing the results of TARGET2 data simulations within the framework of the payment system oversight for several years already. After joining the euro area, Latvijas Banka engaged in the overall oversight of TARGET2 within the Group of authorised overseers (GAO), taking part in the analysis of data extracted from TARGET2 simulator. In October 2013, the overseers participated in the meeting of GAO where they shared their experience with the members of the working group regarding the simulations of the SAMS data made by means of the Simulator BoF-PSS2, as well as presented the project of TARGET2-Latvija data simulation.

## **7.2 Cooperation with other national central banks**

Latvijas Banka convened the Nordic-Baltic annual meeting in Riga on 26 and 27 August 2013. Representatives from the central banks of Denmark, Estonia, Iceland, Latvia, Lithuania, Norway, Finland and Sweden participated in it. The participants of the meeting shared their experience of the achievements of the previous year and presented information about the future plans regarding the oversight of payment and settlement systems. Parties engaged in discussions and gave presentations about various oversight related issues, including the application of the CPSS-IOSCO Principles for financial market infrastructures, insolvency proceedings on payment and settlement systems, retail payments, payment instruments and studies of social costs of payment instruments, payment services regulation, oversight of central counterparties, the expected CSD Regulation, issues of reconciling CSDs, implementation of T2S project, SEPA, role of the national central banks regarding the business continuity requirements for credit institutions, and other topical issues.

In December 2013, the overseers organised a one-day meeting with the representatives of the Central Bank of Armenia, CSD and NASDAQ OMX Armenia, subject to a request by the Central Bank of Armenia, gave a presentation on the issues of securities trading and settlement relevant for the audience and shared the experience of Latvijas Banka regarding the oversight of payment and securities settlement systems.

## **7.3 Cooperation with the FCMC**

Over the year the overseers held a number of meetings with their colleagues from the FCMC and debated about the oversight of payment and securities settlement systems as well as organised a workshop on payment systems, subject to a request of the FCMC, and gave a presentation thereof as well as exchanged experience in other payment system-related issues.

## **8. INFORMATION TO THE PUBLIC**

Information on the development of payment instruments and their infrastructure and payment and securities settlement systems as well as the activities performed by Latvijas Banka with respect to the oversight of payment and securities settlement systems has been published in the "Annual Report of Latvijas Banka", "Financial Stability Report" and on the website of Latvijas Banka. The annual statistics of Latvia's payment and securities settlement systems and payment instruments has also been published in the ECB Statistical Data Warehouse.

## **9. THE PAYMENT AND SECURITIES SETTLEMENT SYSTEM POLICY OF LATVIJAS BANKA**

In 2013, the oversight of payment and securities settlement systems was conducted in accordance with the objectives and tasks stipulated by "The Payment and Securities Settlement System Policy of Latvijas Banka" for each component of the national payment and securities settlement system: systemically important payment and securities settlement systems, clearing and retail payment systems and payment instruments.

Upon joining the Eurosystem along with the changeover to the euro the oversight policy of the ECB became binding on Latvijas Banka. On 11 July 2013, Latvijas Banka took a decision to deem invalid "The Payment and Securities Settlement System Policy of Latvijas Banka" as of 1 January 2014. As of 1 January 2014 Latvijas Banka performs the oversight of payment and securities settlement systems in line with the relevant Eurosystem oversight policy governing the oversight of payment and securities settlement systems. Information on the oversight of payment and securities settlement systems was prepared and updated by Latvijas Banka on its website, providing a general description of the oversight conducted by Latvijas Banka in the capacity of one of a member of the Eurosystem, as well as presenting the objectives and methods of the oversight performed by the Eurosystem.

In view of the fact that "The Payment and Securities Settlement System Policy of Latvijas Banka" had been developed in accordance with the relevant policy of the Eurosystem governing the oversight of payment and securities settlement systems, the repealing of Latvijas Banka policy did not cause notable changes as regards the scope of the oversight responsibilities in Latvia. Latvijas Banka continues to carry out oversight, focussing mainly on systemically important payment and securities settlement systems. The operation of the SAMS was terminated after the euro changeover, whereas TARGET2-Latvija gained in importance since it was used for settling payments related to the monetary policy of the Eurosystem. Upon becoming a fully-fledged member of the Eurosystem, in line the procedures stipulated by the Eurosystem Latvijas Banka intends to be actively involved in the oversight of TARGET2 (for instance, by evaluating changes in the system and analysing its operation by means of the Simulator on a regular basis). Prior to the euro changeover in Latvia Latvijas Banka engaged in the oversight of TARGET2 in the capacity of an observer. The securities settlement system of LCD has retained its systemic importance since it is the sole securities settlement system in this country and securities registered with the LCD are used for the Eurosystem's monetary policy related settlements after the euro changeover; hence the scope of oversight has remained unchanged.

The EKS has maintained its current status of a systemically prominent retail payment system also after the introduction of the euro, and Latvijas Banka continues to perform its oversight. Latvijas Banka proceeds with the oversight of other systems operating in Latvia (e.g. the FDL) and payment instruments, including the assessment of systems, compilation of payment statistics and participation in the ECB's European Forum on the Security of Retail Payments (SecuRe Pay).

The Eurosystem is currently developing new procedures for the assessment of systems in accordance with the new CPSS-IOSCO standards, a requalification of retail payment systems is planned and Latvijas Banka will have to evaluate the EKS in 2014 or in 2015 in accordance with the new methodology developed by the Eurosystem. Substantial

changes are expected in the performance of the oversight of securities market infrastructure associated with a special focus of the EU institutions, including the Eurosystem, on the prevention of risks to contain the impact of future crises and strengthen financial stability. The implementation of T2S Project and market consolidation-related issues will also bring about changes in the oversight practice of the Eurosystem, with Latvijas Banka and other participants of the Eurosystem taking part in its development and implementation.

Latvijas Banka engaged in drafting the new oversight documents of the Eurosystem and provided comments on the relevant projects. In 2013, the Eurosystem adopted the CPSS-IOSCO oversight principles Principles for financial market infrastructures (PFMI) approved in April 2012. To ensure smooth and efficient operation of systemically important payment systems, the ECB has drafted the Regulation on oversight requirements for systemically important payment systems that will fully introduce CPSS-IOSCO PFMI and replace the current Core Principles. The Regulation is currently open for public consultation and is planned to be approved in 2014. As regards retail payment systems, the ECB has updated the Revised oversight framework for retail payment systems, whereby CPSS-IOSCO PFMI are adopted for the retail payment system oversight. At the same time, the adoption of CPSS-IOSCO PFMI for securities settlement systems is to be performed in accordance with the Regulation of the European Parliament and of the Council on improving securities settlement in the European Union and on central securities depositories (CSDs) and amending Directive 98/26/EC since it will fully introduce CPSS-IOSCO PFMI. The Governing Council of the ECB has passed a decision to use CPSS-IOSCO oversight principles and assessment methodology approved in April 2012 by the time the Regulation takes effect.

## APPENDIX. TASKS PERFORMED BY LATVIJAS BANKA IN THE SEPA PROJECT

Latvijas Banka (the overseers) continued to steer the NSWG in 2013, coordinating the cooperation among the representatives of the payment market supply side (the ACBL, *Latvijas Pasts*, First Data Latvia Ltd, JSC *OpusCapita*, Latvian Information and Communications Technology Association (LIKTA) and representatives of the demand side (the Consumer Rights Protection Centre, SMECCC, LDDK, Treasury, Ministry of Finance of the Republic of Latvia and Latvijas Banka). The representatives of the respective institutions and associations coordinated, within the scope of their competence, the current assignments for integration into SEPA.

The MPSWG performed the supervision of the NSWG. In 2013, the overseers carried out a number of activities to prepare for one of the most significant tasks of the SEPA implementation – to ensure transition from the payments in lats to SEPA credit transfers in euro along with the euro changeover. The SEPA-related task "To implement SEPA credit transfers" has been incorporated into the Plan of the MPSWG and Annex 1 "Action Plan for the Introduction of the Single European Currency in Latvia" to Latvia's National Euro Changeover Plan, with 1 January 2014 set as deadline for its performance. The overseers monitored the implementation of measures to prepare for the changeover to SEPA credit transfers and conducted a survey whereby Latvia's credit institutions, the Treasury, *Latvijas Pasts* and Latvijas Banka confirmed their readiness to replace all customer credit transfers in lats by SEPA credit transfers in euro as of 1 January 2014 (excluding urgent payments and payments via TARGET2).

Credit transfers in lats accounted for about 94% of all credit transfers executed in Latvia in 2013. Overall, credit transfers account for almost half of all payments made in Latvia.

As regards SEPA communication process, the overseers implemented several SEPA communication activities in 2013, inter alia maintained and updated SEPA Latvia website [www.sepalatvija.lv](http://www.sepalatvija.lv), were involved in the preparation of a video material about SEPA "The ABC of the Economy: What is SEPA?", published on the website and demonstrated by Latvia's Television. At the end of the year Latvijas Banka published SEPA infographics and informational press release on SEPA and changes taking place in the area of payments as of 1 January 2014.

The overseers were in charge of the drafting of Latvia's National SEPA Plan, Version 5.0. Latvia's National SEPA Plan was amended by incorporating the following information:

- the decision taken by the participants of SEPA Project to apply the derogation, stipulated in the SEPA Regulation, and waive the requirement of using XML message standard in customer-to-bank domain and bank-to-customer domain until 1 February 2016;
- the development of the relevant national standard compliant with the requirements of XML message standard to be completed by the end of 2013;
- the subjects of SEPA Creditor Identifier and practical aspects of maintenance in the databases of the RE;
- the issue of reaching agreement by Latvian credit institutions, companies and JSC *OpusCapita* until 1 January 2014 on the most efficient solution to be used for the replacement of the national direct debit payments by 1 January 2015.

On 11 October, the NSWG approved draft Version 5.0 of Latvia's National SEPA Plan and MPSWG approved it in the written consultation on 28 October.

In 2013, the overseers produced four progress reports of the NSWG for submission to the MPSWG.

To monitor the progress of implementing SEPA payments in the payment system of Latvia, the overseers proceeded with the compilation of the following SEPA indicators: SEPA credit transfers, SEPA direct debit payments and SEPA Card Framework. In September, the overseers drafted a progress report on the SEPA Project in Latvia and NSWG approved it during the written consultation.

In the fourth quarter of 2013, SEPA credit transfers stood at 1 416 thousand (98.2%) of credit transfers executed in euro (excluding credit transfers in euro transmitted to third countries and urgent credit transfers in euro).

The four main indicators of the SEPA Card Framework in Latvia at the end of 2013 were as follows: 1) 1 177 (100%) ATMs of Latvia's banks had migrated to Europay-Mastercard-Visa (EMV) and were compliant with the SEPA requirements; 2) 25.9 thousand (100%) POS terminals had migrated to EMV; 3) 1 849.9 thousand (99.6%) debit cards were compliant with the EMV Standard and SEPA requirements; and 4) 345.7 thousand (99.3%) credit cards were compliant with the EMV Standard and SEPA requirements.

In 2013, 91.1% of all euro and lats payments executed with cards were based on the EMV Standard. At the end of 2013, 99.8% of Latvian e-merchants used *3D Secure* technologies in e-commerce environment and 54.6% of all cards were registered for *3D Secure* technology. In the second half of 2013, 83.2% of domestic e-commerce transactions were consistent with the requirements of *3D Secure* technologies.

In 2013, the overseers were involved in the following key activities of the SEPA Project.

- They coordinated the compilation of the responses to the survey on the migration of public authorities to SEPA and submission to the EC. Subject to the results, public authorities execute credit transfers in euro in line with the SEPA requirements and are ready to replace their lats payments with SEPA credit transfers upon the changeover to the euro. Latvijas Banka, the Treasury, SSIA, SRS and the Ministry of Finance of the Republic of Latvia participated in the survey.
- On 13 July 2013, the overseers together with the representatives of the FCMC participated in a technical discussion about the SEPA Regulation, organised by the EC. During the discussion competent authorities exchanged opinions and discussed the most topical issues of interpretation and application of the SEPA Regulation.
- The overseers provided advice to the RE on practical aspects of implementing the SEPA Creditor Identifier. Information on the SEPA Creditor Identifier will be publicly available along with other information on a legal person of Latvia (the registration number, name, registered address). The SEPA Creditor Identifier will be developed in line with the structure of the SEPA Creditor Identifier. The SEPA Creditor Identifier will be maintained in the databases of the RE as of the euro changeover day.
- The overseers advised *Latvijas Pasts* on the necessary measures to be taken to ensure efficient migration to SEPA credit transfers as of 1 January 2014.
- The overseers, in cooperation with the FCMC, advised market participants actively on the requirements stipulated in the SEPA Regulation and Regulation (EC) No 924/2009

of the European Parliament and of the Council on cross-border payments in the Community, repealing Regulation (EC) No 2560/2001, applicable as of 1 November 2009.

The overseers continued to coordinate debates about the implementation of SEPA direct debit payments in Latvia. In September, a discussion was held among the representatives of the JSC *OpusCapita*, ACBL and LDDK, resulting in a decision to agree by 1 January 2014 on an alternative SEPA requirements-compliant solution to be used for the replacement of the national direct debit payments until 2015. At the end of the year, the *OpusCapita*, ACBL and LDDK decided not to convert the national direct debit payments into SEPA credit transfers, albeit to replace them by SEPA credit transfers combined with e-invoicing until 2015, similarly to the process of converting the national direct debit payments in Finland and Estonia.

The overseers convened a meeting of the SEPA Card Framework Subgroup of the NSWG on 24 April. The SEPA Card Framework Subgroup addressed the issue of liability shift due to the use of counterfeit payment cards raised by Latvian Merchant Association, continued the work commenced in the previous period, as well as agreed to revise recommendations for the card framework stakeholders "On Changes in the Procedures for Accepting Payment Cards VISA and MasterCard".

On 24 September 2013, the SEPA Card Framework Subgroup of the NSWG organised a SEPA seminar for the stakeholders of the following merchant associations: the Latvian Association of Hotels and Restaurants, the Latvian Merchant Association, the Latvian Food Retailers Association, the Latvian Association of Fuel Traders and the Latvian Association of Pharmacists. Information on both the implementation of SEPA standards and topical issues concerning the changeover to the euro were presented at the workshops.

The overseer from Latvijas Banka participated in the regular meetings of the Forum of NSWGs organised by the EC on 18 June and 14 November 2013. The representative of Latvia made presentations on the implementation of Latvia's National SEPA Plan and progress of the SEPA Project in Latvia. The participants of the Forum debated about the migration process of SEPA core products in each Member State and SEPA governance issues.