

MEMORANDUM OF UNDERSTANDING ON THE MANAGEMENT OF FINANCIAL CRISES

PRELIMINARY STATEMENT

Taking into account the importance of cooperation while managing a systemic financial crisis, considering the need for regulating cooperation between the Ministry of Finance, Eesti Pank and the Financial Supervision Authority (hereinafter referred to as the Parties, and separately, the Party), and specifying coordination in cases of a systemic financial crisis without changing the legal status of the Parties and restricting their activities, which are based on legislation, the Ministry of Finance, represented by Aivar Sõerd, the Minister of Finance; Eesti Pank, represented by Andres Lipstok, the Governor of Eesti Pank; and the Financial Supervision Authority, represented by Raul Malmsten, the Chairman of the Board, have concluded this Memorandum of Understanding (hereinafter referred to as the Memorandum) as follows.

1. GENERAL PROVISIONS

1.1 The Memorandum shall specify the responsibilities of the Parties and the principles of coordination in cases of systemic financial crises.

1.1.1 According to the Memorandum, a systemic financial crisis shall be defined as a situation when the functioning of the financial system is seriously interrupted; e.g. due to liquidity and/or solvency problems of one or several credit institutions, disturbances in the payment and settlement systems, or the failure of financial markets.

1.1.2 According to their competence and jurisdiction, the Parties shall compile and exchange their assessment of the systemic nature of the financial crisis. While assessing the systemic nature of the financial crisis, the Parties shall apply different criteria, including the market share of a problematic credit institution, the impact on other financial institutions, the general situation of the financial markets etc.

1.2 The objective of the Memorandum is to support the process of managing a possible systemic financial crisis in such a way that minimizes the damage that might be caused to the society and to the creditors of the credit institution experiencing solvency problems.

1.3 The support of the state for providing liquidity and/or capital shall be offered in order to manage a financial crisis in cooperation with Eesti Pank or separately only in cases when the private sector solutions tend to be insufficient or ineffective. The primary liability for the damage caused by the financial crisis shall be sustained by the owners, the management and the supervisory board of the problematic credit institution.

1.4 According to the framework of the Memorandum, only such financial crises that are related to the activities of the credit institutions, their subsidiaries and parent companies operating in Estonia shall be subject to treatment.

1.5 A cross-border financial crisis shall be managed in cooperation with the corresponding parties of other countries. The coordination of a cross-border financial crisis is pursuant to the bilateral or multilateral agreements between Parties and the corresponding parties of other states or associations of states.

1.6 The Memorandum shall not apply on cooperation between the Parties in everyday situations, including crisis prevention measures (excl. any necessary preparations for the management of a potential financial crisis).

1.7 The activities of the Parties shall be based on the legal rights, duties, and responsibilities specified by legislation as well as on the division of their roles and tasks determined by the Memorandum.

1.8 The Memorandum shall contribute to the national cooperation agreement concluded between the Parties on 1 November 2002.

2. TASKS AND RESPONSIBILITIES OF THE PARTIES

2.1 In Estonia, financial crises shall be managed by the Financial Supervision Authority, Eesti Pank, and the Ministry of Finance.

2.2 In cases where it is deemed necessary, the Parties shall involve a third party as an independent mediator in the process of managing a financial crisis. The task of an independent mediator shall be to assist the Parties in finding new strong reliable owners for the problematic credit institution.

2.3 Tasks and responsibilities of the Financial Supervision Authority

2.3.1 In the process of financial crisis management, the tasks and responsibilities of the Financial Supervision Authority shall include assessment of the situation, application of supervisory measures, exchange of information with owners, and exchange of information and joint actions with the financial supervision authorities of the other countries involved.

2.3.1.1 When assessing a crisis, the Financial Supervision Authority shall constantly monitor the financial situation of the problematic credit institution and evaluate the amount of possible liquidity assistance and capital injection.

2.3.1.2 The Financial Supervision Authority shall monitor the willingness and ability of the owners to allocate capital and liquid funds within the consolidated group, or obtain additional funds.

2.3.2 The Financial Supervision Authority shall promptly notify the other Parties of any changes in a crisis situation aiming to ensure implementation of crisis management measures in a way that minimises disruptions in the financial system and optimises costs for the state.

2.4 Tasks and responsibilities of Eesti Pank

2.4.1 In the process of crisis management, the main task of Eesti Pank is to grant emergency liquidity assistance to problematic credit institutions.

2.4.2 Eesti Pank may grant emergency liquidity assistance against sufficient collateral to a credit institution that is deemed solvent according to the estimation of Eesti Pank. Eesti Pank may also grant supplementary liquidity support in the form of emergency liquidity assistance to ensure a smooth process of restoring solvency.

2.4.3 Eesti Pank shall notify the Parties immediately of any disturbances to the payment and settlement systems which have a significant impact on the functioning of the financial system.

2.5 Tasks and responsibilities of the Ministry of Finance

2.5.1 In a situation when the Minister of Finance, the Government of the Republic or the Riigikogu (the Parliament) have decided to rescue or re-structure a credit institution with signs of a systemic crisis, the task of the Ministry of Finance shall be to arrange the legislative proceedings for allocating the financial funds pursuant to the procedure and scope of application designated in legislation.

2.5.2 According to the resolution referred to in 2.5.1 of the Memorandum, contributions in the form of equity capital can be made to rescue or re-structure a credit institution, or to grant loans and guarantees for loans, or to invest the funds in a financially troubled institution in a different form pursuant to legislative provisions.

2.5.3 In order to rescue or re-structure a credit institution, the Government funds shall be applied first along with the funds of the private sector and the relevant funds of Eesti Pank. If these measures turn out to be inefficient, they shall be applied separately.

3. COORDINATION

3.1 A Party that considers that there is a potential systemic financial crisis shall inform the other Parties of its assessment and call a joint committee meeting in cases where it deems such action necessary.

3.2 The Joint Committee

3.2.1 The Joint Committee is a temporary high-level committee consisting of representatives of the Parties to coordinate the management of a systemic crisis.

3.2.2 The duties of the Joint Committee shall be as follows:

3.2.2.1 coordinate the Parties' assessments on whether a systemic crisis is taking place;

3.2.2.2 appoint or re-appoint the Party who shall take the lead in the process of crisis management;

3.2.2.3 ensure a smooth exchange of information and coordinate the activities between the Parties (including the choice and scope of applied measures);

3.2.2.4 if necessary, appoint an independent mediator;

3.2.2.5 if necessary, coordinate communication according to the principles provided for by Subsection 6 of Section 3 of the Memorandum.

3.2.3 The Joint Committee shall report to the Minister of Finance, the Governor of Eesti Pank and the Chairman of the Management Board of the Financial Supervision Authority.

3.2.4 The activities of the Joint Committee shall be regarded as finished by agreement of the Parties.

3.3 The Parties shall inform the other Parties of any changes in their legislation or work arrangements concerning their areas of responsibility in relation to crisis management.

3.4 In order to ensure a timely transfer of relevant information leading to necessary activities, the Parties shall compile and update the common national list of contact persons, which is annexed to the current Memorandum.

3.5 The Parties shall regularly conduct national crisis simulation exercises and stress tests.

3.6 The Parties shall coordinate the scope and content of the information delivered to the public with each other in advance. In addition, they shall approve any communication with international organisations, and in cases of need, the cooperation with the institutions and committees of the European Union.

4. EXCHANGE OF INFORMATION

4.1 The current Memorandum shall involve only such exchange of information that is performed in the context of an emerged or potential (systemic) financial crisis.

4.2 According to the availability of information, pursuant to their fields of competence, the Parties shall deliver whatever information is necessary to each other for the efficient management of a crisis. The exchange of information between the Parties shall include the quantitative indicators of the problematic credit institution as well as the qualitative assessment of the suitability and effects of the potential measures.

4.3 The Parties shall specify the circle of outside domestic and foreign institutions to share information with during a financial crisis. The cross-border exchange of information is pursuant to the principle that the Parties shall communicate with their respective counterparts (the central bank shall communicate with other central banks, the supervision authority with other

supervision authorities, and the ministry with other ministries). When necessary, they may communicate directly, informing the relevant Party in advance when possible.

5. CONFIDENTIALITY

5.1 The exchange of information between the Parties is confidential by nature, as specified in the framework of the Memorandum. The Parties shall ensure the confidentiality of information within the framework of enacted legislation.

5.2 The Parties shall ensure that all persons who come across the corresponding information shall be obliged to meet the requirements of confidentiality.

5.3 The exchange of information performed within the framework of the Memorandum shall be applied only in cases of achieving the objective of the Memorandum. When communicating sensitive information to third persons, those offering the information, as well as the receivers of the information, should be notified of this in advance.

6. VALIDITY OF THE MEMORANDUM

The Memorandum has been concluded without a set term and shall enter into force upon the signatures of all the Parties.

7. AMENDMENTS TO THE MEMORANDUM

At least once every three years, the Parties shall carry out an assessment of the Memorandum to determine whether or not it is up-to-date, and if necessary, they shall amend it. The annex to the Memorandum shall be reviewed at least once a year, and it shall be updated in case of need.

The Ministry of Finance
Aivar Sõerd
Minister
5 December 2006

Eesti Pank
Andres Lipstok
President
5 December 2006

The Financial Supervision Authority
Raul Malmstein
Chairman of the Board
5 December 2006