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I Address of the Management Board



Finantsinspektsiooni juhatuse: Andre Nõmm, Kilvar Kessler (juhatuse esimees) ja Andres Kurgpõld

Dear Reader,

The regulated financial market in Estonia has been overall sound in 2014. Market participants were well capitalized and appropriately prudent. They encountered numerous complex new legal acts and resulting tasks that put both the market and the supervisors to the test. This Management Report provides a brief overview of major risks that affected the Estonian financial sector as well as of main lines of action of the financial supervision in the financial year and in the coming years.

Participants in the Estonian financial market were influenced by tightening international developments in nearby regions, namely the conflict in Ukraine, as well as by low euro area interest rates, high household debts and the risk of overheating real estate markets in Scandinavian countries.

Scandinavian banks capture the majority of Estonian financial sector. The crystallisation of risks in Nordic countries affects – through the solvency of parent banks – also the performance of financial markets in Estonia. Similar to the last year, the capital requirements imposed by the Financial

Supervision Authority in respect of major banks operating in Estonia in order to mitigate the risks were 30% higher than the requirements applied by default. Banks meet these regulatory prudential norms with a good margin.

Tightened international developments fed the insecurity that triggered irrational and hectic financial behaviour of investors and depositors. On the other hand, the imposition of international sanctions affected the ability of economic entities to meet their obligations in respect of financial intermediaries. In the aftermath of this tense situation, financial intermediaries were required to apply enhanced due diligence in complying with the imposed financial sanctions, in order to avoid the situation where persons subject to sanctions could take advantage of the sector.

In 2014, the Financial Supervision Authority drew the attention of market participants to the need of complying with international sanctions with special care. In addition, our experts carried out on-site inspections regarding the functioning of processes and systems of financial intermediaries within the scope of tackling money laundering and preventing terrorist financing.

Low interest rates are in general good news for borrowers, but not always for financial intermediaries who may have long-term contractual obligations to pay higher interests to their clients. In 2014, the Financial Supervision Authority together with the European Insurance and Occupational Pensions Authority (EIOPA) carried out stress tests in respect of insurers, evaluating the resilience of insurance sector to the persistence of low interest rates, considering the new insurance framework that enters into force in 2016. Estonian insurers who participated in this stress testing passed the test of new regulation; however, the extended period of low interest rates would have a major adverse impact on them.

The Financial Supervision Authority contributed to the set up and launching of the euro area Single Supervisory Mechanism (SSM) in the field of prudential supervision of banks. In order to draw a coherent picture of the health and situation of euro area banking sector, the European Central Bank together with, among others, the Financial Supervision Authority carried out the Comprehensive Assessment of the assets of major banks in 2014, for better planning of future actions. Three Estonian banks that participated in this assessment passed the prescribed target by a wide margin.

In the area of consumer protection, the Financial Supervision Authority concluded that the infringement of rules by unregulated consumer credit providers led to the distortion of competition and the violation of borrowers' rights. A regulative solution was achieved in this issue in cooperation with partners from various ministries and the parliament.

The Financial Supervision Authority mapped the achievements in the area of consumer education as well as relevant actions of its partners in neighbouring countries. In order to enhance the public awareness of financial services, the respective function was reorganised and the focus was shifted towards dealing with individual issues for the support of core activities of financial supervision.

The Financial Supervision Authority examined the asset investments of conservative pension funds and concluded that these investments complied with the requirements provided by the Investment Funds Act. Also, the inspections covered the existence of the assets of mandatory pension funds and whether they were deposited in depository banks.

As the activities of the Financial Supervision Authority are increasingly intertwined with the activities of relevant EU agencies, it adjusted its planning procedures respectively. Main challenges during the next financial year 2015 include the implementation of supervision of credit providers and intermediaries; set up and launching of the recovery function that is independent from the banking supervision, and the integration of this recovery function with the respective European system; integration with the euro area Single Supervisory Mechanism; and linking the consumer education function with market supervision and enforcement activities. In order to enhance the efficiency of our performance, the focus on the implementation of law will be strengthened. Internal rules of the the Financial Supervision Authority need to be analysed, revised and adjusted due to changes in the environment.

We will put a greater emphasis on smaller banks, insurers and actors on securities markets. As the reporting by market participants is one of the main inputs to our prudential supervision, we will examine the accuracy of these reports. In order to preserve the strong credibility of the Estonian financial sector, we will continue our comprehensive tasks in the prevention of money laundering and terrorist financing as well as in the area of international sanctions.

Thank you and enjoy the reading!

Management Board of the Estonian Financial Supervision Authority

2 Confirmation of the Management Board



In Tallinn, 20 March 2015

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

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

- Management Report on pages 6 to 28;
- Annual Report of Revenues and Expenditures on pages 29 to 32;
- Balance Sheet on page 33;
- Auditor's Report on page 34.

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

Kilvar Kessler

Andres Kurgpöld

Andre Nõmm



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Financial Supervision Authority's Management Report

3.1. Brief overview of the Financial Supervision Authority



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

Activities of the FSA are financed through supervisory fees and procedural fees that are paid by entities subject to financial supervision.

The FSA is a member of the European Single Supervisory Mechanism (SSM) that performs the supervision of significant banks and respective groups as of 4 November 2014.

The FSA's activities are planned and its management is controlled by the Supervisory Board. The Supervisory Board has six members. The Minister of Finance is acting as the Chairman by virtue of office.

Everyday activities of the FSA are directed by the Management Board consisting of 3 members. The new composition of members commenced its activities in January 2014. The Board as a collective management body makes decisions by majority vote, and the activities of the Management Board are directed by the Chairman.

Supervisory activities of the FSA are divided into market and business conduct supervision activities and prudential supervision activities. Prudential supervision is aimed at analysing the risks and business continuity of financial institutions, whereas market and business conduct supervision is aimed at ensuring the transparency, credibility and effectiveness of financial services.

Mission of the FSA – to ensure the financial stability and to protect clients and investors.

Vision of the FSA – the stable Estonian financial market that is integrated with the common market of the European Union characterized by transparent and determined supervision.

3.2. Management and organisation

3.2.1. Activities of the Supervisory Board

As at 31 December 2014, the Supervisory Board of the FSA included:

Chairman:

- **Maris Lauri**, Minister of Finance

Members:

- **Ardo Hansson**, Governor of the Eesti Pank
- **Aivo Adamson**, Director General of the Estonian Road Administration
- **Madis Müller**, Deputy Governor of the Eesti Pank
- **Valdo Randpere**, Member of *Riigikogu*
- **Veiko Tali**, Secretary-General at the Ministry of Finance

Resolutions of the Supervisory Board

In 2014, the Supervisory Board held five meetings.

The Supervisory Board approved the 2014 Annual Report and transferred the operational profit of the financial year within the amount of € 211,701.91 into the reserve of the FSA.

The Supervisory Board approved the 2015 budget of the FSA in the amount of € 6,357,000 and presented a proposal to the Minister of Finance for setting the 2015 rates for the supervisory fee shares.

Considering the probability that the FSA will be charged with additional tasks in 2015, the Supervisory Board held a discussion in November 2014 on the issues related to changing the bases for the design of organisational structure and increasing the number of positions, and linked the respective resolutions to the adoption of specific legislation.

3.2.2. Activities of the Management Board

As at 31 December 2014, the Management Board of the Financial Supervision Authority included:

Chairman:

- **Kilvar Kessler**

Members:

- **Andre Nõmm**
- **Andres Kurgpõld**

Resolutions of the Management Board

In 2014, the Management Board held 57 meetings and adopted 83 administrative decisions, including 6 injunctions. In one occasion, the Management Board adopted a decision to enforce a penalty payment in respect of a supervised entity. Licenses or supplementary licenses were issued to 5 financial institutions. In one occasion all licenses issued to a supervised entity were revoked and in another occasion a supplementary license issued to a supervised entity was revoked. License application was refused in one occasion.

In the area of prudential supervision, one of the major challenges in 2014 was the smooth organisation of Comprehensive Assessment in cooperation with the European Central Bank before the scheduled start of common banking supervision. This task required the performance of extraordinary audits in three major Estonian banks.

Management Board sought to increase the due diligence of supervised entities in meeting anti-money laundering requirements, and focused on the transactions of non-resident clients. The area of anti-money laundering required particularly high attention from the business conduct supervision division in 2014.

Inspection activities were continuously focused on the examination whether conservative pension funds adhered to rating restrictions as well as on expenses and fees at the expense of mandatory pension funds.

Management Board contributed to the transposition of recovery framework into Estonian laws as well as to the shaping of supervisory framework for credit providers and intermediaries.

Members of the Management Board – areas of responsibility in 2014

Kilvar Kessler, Chairman of the Management Board, was responsible for the governance of the FSA, organising the activities of the Management Board, and effective functioning of all supervisory activities, including the activities in the SSM Supervisory Board resulting from the Council Regulation (EU) No 1024/2013¹. He was also responsible for institutional development, coordination of national cooperation, coordination of international and public relations as well as international cooperation, organising the activities of internal audit function, organising staff training, coordination of regulatory legal issues, developing the regulative environment of the financial sector, developing statements on financial and supervisory policies, and promoting communication activities and consumer education area.

Andre Nõmm, Member of the Management Board, was responsible for the functioning and development of Market and Business Conduct Supervision and Administrative Services, including for the supervision of financial services and securities market, as well as for developing the regulative environment of the financial sector, and preparing statements on financial and supervisory policies in his area of responsibility. He was also responsible for the prevention of money laundering and terrorist financing, organising the notification procedures in case of cross-border services, coordination of international cooperation in his area of responsibility, organising the budgetary process of the FSA, functioning and development of administrative services, and development and implementation of IT information security policies and procedures.

Andres Kurgpõld, Member of the Management Board, was responsible for the functioning and development of Prudential Supervision, including for the supervision of credit institutions, insurers, investment firms and other supervised financial institutions, focusing on monitoring the risks of supervised entities, their solvency and other aspects of prudential supervision. He was also responsible for organising the process of market entry and exit of financial institutions, adherence to prudential norms by managers and holders of qualifying holdings, developing the regulative environment of the financial sector, and preparing statements on financial and supervisory policies in his area of responsibility, focusing on prudential regulation for supervised entities. His area of responsibility included international cooperation in his area of responsibility and the collection and development of regular reporting.

¹ Council Regulation (EU) No 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions

3.2.3. Organisational development, personnel policy and training

72 positions out of 80 created in the FSA were staffed as at 31 December 2014. Employment contracts had been temporarily suspended with 4 employees for the duration of parental leave. In 2014, the FSA recruited 8 new employees and it witnessed the departure of 9 employees. The average age of the FSA's employees was 37.9 and the average length of service at the Authority was 9.7 years. The core personnel included lawyers, financial analysts and risk managers. All employees of the FSA are with higher education qualifications. As at the end of 2014, 5 employees were enrolled in the Master's Study Program and 2 in the Doctoral Study Program.

Training of employees

In 2014, employees of the FSA participated in both national and international supervision-focused training events. Also, in-house professional training sessions were organised.

In 2014, the average cost of international training amounted to € 1079 per employee and that of national training amounted to € 251 per employee.

The profile of employees by age

Age	Number of employees	%
20–29	14	19.4
30–39	26	36.1
40–49	23	31.9
50–59	8	11.1
60–65	1	1.4

The profile of employees by length of service at the FSA

Years	Number of employees	%
Up to 5 years	23	31.9
6–10 years	16	22.2
11–15 years	13	18.1
16–20 years	14	19.4
21–23 years	6	8.3

3.2.4. Summary by the Internal Auditor

The position of an Internal Auditor of the Financial Supervision Authority has been created pursuant to the Financial Supervision Authority Act. The Internal Auditor submits reports to the Management Board and to the Supervisory Board. Management Board approves the Internal Auditor's strategic plan for four years as well as more detailed working plans for each quarter. The Internal Auditor presents quarterly reports to the Management Board on his activities and the results of audits. In addition, he reports on his activities to the Supervisory Board at least once a year.

The Internal Auditor audited mainly the following two areas in 2014:

- Core activity of the Financial Supervision Authority, i.e. carrying out financial supervision;
- The functioning and organisation of work within the FSA.

In evaluating the organisation of financial supervision, the Internal Auditor examined the functioning of supervision and international cooperation as well as the scope of procedures and processes in various areas and aspects. When auditing the functioning and organisation of work within the Authority, the Internal Auditor evaluated the adherence of document management and preparation of business trips to internal rules.

The Internal Auditor considered that the level of discipline was continuously high in 2014 when implementing decisions of the Supervisory Board and the Management Board. Management and control systems of the FSA functioned, to a large extent, as might have been reasonably expected.

3.3. Supervisory activities

3.3.1. Issuing new licenses and registering prospectuses of investment and pension funds and other issuers

Issuance and revocation of licenses

In 2014, the FSA issued licenses to four companies, and revoked all licenses issued to a supervised entity in one occasion and a supplementary licence for investment consultation services in another occasion.

The FSA issued a fund manager license to FB Asset Management AS. This license entitles the company to manage investment funds. The license was issued with a restriction – FB Asset Management AS has no right to manage UCITS funds in the meaning of the Investment Funds Act.

The FSA issued an alternative investment fund manager license to EfTEN Capital AS, allowing EfTEN Capital AS to manage alternative investments funds in the meaning of the Alternative Investment Fund Managers Directive (Directive 2011/61/EU of the European Parliament and of the Council). As restrictions have been imposed to the activities of alternative investment fund managers, the FSA revoked the additional license of EfTEN Capital AS – as requested by EfTEN Capital AS – that allowed the supervised entity to provide investment consultation services.

According to the Payment Institutions and E-money Institutions Act, the FSA issued a payment institution license to TavexWise AS. This license allows TavexWise AS to provide money remittance services. Money remittance is a payment service where funds are transferred from the payer to the payee or a payment service provider acting on behalf of the payee without opening a payment account in the name of the payer or payee.

The FSA authorized the commercial association Kambja Hoiu-Laenuühistu to use the exemption provided by the Payment Institutions and E-money Institutions Act. This exemption allows the commercial association Kambja Hoiu-Laenuühistu to provide money remittance services. The exemption can be applied under simplified criteria and provided that the average total amount of payment transactions made within the preceding twelve months does not exceed one million EUR a month.

The FSA revoked the licenses issued to ERGO Funds AS for the management of mandatory and voluntary funded pensions. Licenses were revoked pursuant to a request submitted by ERGO Funds AS, as the operator wanted to cease its activities as a fund manager.

Due to material shortcomings in submitted documents, the FSA returned the application for a licence in case of three companies. In addition, the FSA refused a license application of a company that applied for a payment institution license.

Registration of investment and pension funds

In 2014, the FSA registered the terms and conditions of 2 new investment funds – 4Times Meta Fond and FB Income Fund – and accorded the articles of association of the investment fund EfTEN Kinnisvarafond II AS (incorporated as a public limited company).

The year 2014 witnessed no new market entries by voluntary or mandatory pension funds.

The FSA registered the amendments of terms and conditions of an investment fund in one occasion in 2014. The FSA verified the completeness, clarity and coherence with legislation of terms and conditions when registering the amendments.

The FSA authorized the merger of Swedbank Venemaa Aktsiafond and Swedbank Kesk-Aasia Aktsiafond in 2014. Trigon Arenevate Turgude Agrisektori Fond was authorized to merge with Trigon Arenevate Turgude Finantssektori Fond. ERGO Funds AS was authorized to surrender its pension funds management business to Nordea Pensions Estonia AS.

Qualifying holding proceedings

Persons pursuing to acquire a qualifying holding in a financial institution that is authorised in Estonia must meet the so-called fit&proper criteria.

In 2014, the FSA performed 3 qualifying holding proceedings. OÜ Avaron Partners was authorized to acquire a direct (and controlling) qualifying holding of over 50% in the fund management company AS Avaron Asset Management. Wealth Bakery OY and Markku Malkamäki were authorized to acquire an indirect qualifying holding in the fund management company Northern Star AS.

Due to material shortcomings revealed during the procedure, four persons waived their plans to acquire a qualifying holding.

Branch licenses (freedom of establishment)

The following branch was established by a EU Member State's financial institution in Estonia in 2014: Nordea Bank AB. The establishment was related to the internal reorganization of Nordea Bank AB (publ): activities, assets and liabilities of the former Nordea Bank Finland Plc Estonian Branch were transferred to the Nordea Bank AB Estonian Branch (established at the beginning of 2014).

The insurer Codan Forsikring A/S Estonian Branch (RSA Kindlustus) transferred its insurance portfolio and business to the UAB DK „PZU Lietuva“ Estonian Branch and is being liquidated.

JLT Baltic GmbH Estonian Branch was entered into the FSA list of branches of foreign insurance brokers.

Registration of prospectuses

In 2014, the FSA registered the prospectus for public offering and listing of shares of Arco Vara AS pursuant to the requirements provided by the Prospectus Directive (directly applicable EU Directive). The prospectus of AS Baltika was registered under to the requirements provided by the regulation of the Minister of Finance, as the respective exemption is applicable to the public offer of AS Baltika's convertible bonds.

In 2014, the FSA received 57 notifications on public offers that were registered in other EU countries and offered on a cross-border basis also in Estonia. These notifications were aimed at enabling to offer in Estonia publicly offered securities that were initially registered in another EU country.

Inclusion into and deletion from the list of insurance intermediaries

In Estonia, insurance intermediaries include insurance brokers and insurance agents. Insurance brokers represent the interests of policyholders. An insurance agent mediating services of a specific insurer represents the interest of that insurer. Insurance agents are included into the list of insurance agents by the insurance company represented by the agent.

Insurance intermediaries in Estonia

	Number of insurance intermediaries, 31.12.2014	Number of insurance intermediaries, 31.12.2013
Insurance brokers	39	35
Insurance agents	460	502
Branches of foreign insurance brokers	6	5

In 2014, the FSA included 4 new Estonian-based insurance brokers into the list of insurance intermediaries – Vector Kindlustusmaakler OÜ, RW Kindlustusmaakler OÜ, Ultima Kindlustusmaakler OÜ, AID Kindlustusmaakler OÜ.

Provision of cross-border financial services

Financial institutions authorised in other EU Member States need not apply to the Financial Supervision Authority for a license to provide financial services in Estonia. The provision of cross-border services may commence after the foreign supervisory agency has informed the Financial Supervision

Authority of the financial institution's wish to offer its services in Estonia and has communicated the information required by legislation.

In 2014, the growth in the number of providers of cross-border services continued.

Providers of cross-border services in Estonia²

	Number of providers, 31.12.2014	Number of providers, 31.12.2013
Banking services	302	288
Investment services	1,639	1,393
Non-life insurance services	459	431
Life insurance services	103	99
Insurance broker services	933	923
Insurance agent services	1,450	1,486
Fund management services	43	20
Investment funds	110	63
E-money services	47	41
Payment services	215	174

² Pursuant to the Insurance Mediation Directive 2002/92/EC, the cross-border provision of services by insurance intermediaries is simplified and insurance intermediaries have no obligation to inform the country of destination before the provision of services. Thus, the data presented in this table includes only those insurance intermediaries who have been notified to the Financial Supervision Authority by the financial supervisor of the country of origin.

3.3.2. Risk analysis of market participants, monitoring of their activities and on-site inspections

The FSA is charged with the task of contributing to the efficiency of the Estonian financial sector, the avoidance of systemic risks, and the prevention of the use of the financial system for criminal ends. One of the operational priorities of the FSA is thus the analysis of risks and monitoring of the activities of market participants, primarily for the prevention of any insolvency situations and timely implementation of specific supervisory measures.

Credit institutions

As usual, the risk analysis of credit institutions performed by the FSA was based on traditional quarterly reports in 2014.

Similarly to previous years, the FSA prepared its supervisory evaluation of banks in the framework of the Supervisory Review Evaluation Process (SREP). As a result of SREP, the FSA can set an additional capital requirement for a credit institution above the minimum capital requirement.

The additional capital requirement of the banking sector under Pillar 2 (one of the components of SREP) amounted to € 226.6 million in 2014. The additional capital requirement under Pillar 2 was 29.4% higher than under Pillar 1 for two major banks operating in Estonian market, and 30.6% higher in case of smaller banks. The FSA considers the capitalisation level of credit institutions that operate in Estonia to be strong and adequate for regulative requirements. All three Estonian credit institutions that participated in the Comprehensive Assessment (CA) performed in 2014 under the leadership of the European Central Bank passed this exercise with flying colours.

Significant banks in the meaning of the European Single Supervisory Mechanism (SSM) were subjected to stress testing in 2014 in order to evaluate the capitalization level of credit institutions and their resilience to crises. Strength testing covered a conservative crisis scenario that showed that potential negative situations would have no effect on the capital adequacy of systemically important banks in Estonia. Potential additional loan losses could be covered through interest income or existing capital buffers, and the effect on the capital adequacy indicator of these banks remained under the level on one percentage point.

In 2014, the FSA conducted besides other supervisory activities also on-site inspections in 9 credit institutions and branches.

These on-site inspections covered the following areas:

- Compliance with the requirements of responsible lending;
- Activities of the depository;
- Compliance with the provisions of the Money Laundering and Terrorist Financing Prevention Act;
- Performance of assessment obligations when concluding an investment deposit contract, which are related to the suitability of investment deposit;
- Corporate governance;
- Management of operational risk;
- Functioning of internal audit;
- Credit activities and the management of credit risk, quality of loan portfolio;
- Liquidity management and raising of resources;
- Management of investments;
- Handling of transaction orders issued by clients.

As a result of on-site inspections in the area of prudential supervision, the FSA discovered several deficiencies in the business arrangement of credit institutions and requested a schedule for the elimination of these deficiencies from 4 credit institutions, in order to mitigate the existing risks as soon as possible.

As far as the prevention of money laundering and terrorist financing is concerned, the supervisory activities performed in 2014 in respect of credit institutions and branches were aimed at mapping all crosscutting specific risks in this sector.

On-site inspections in respect of 4 market participants examined whether and how they complied with legislative requirements when establishing business relations with high risk clients, including the performance of subsequent monitoring of clients' activities and notification of potential risks. As a result of these inspections, the FSA requested from all 4 supervised entities to complement their internal rules on the prevention of money laundering and terrorist financing and to amend their work arrangement, in order to ensure better compliance with legislative norms.

The adherence to responsible lending principles was examined in 2 credit institutions. The FSA checked whether these banks assessed the solvency of their clients before making a decision regarding the loan. As a result of these inspections, the FSA requested these two market participants to clarify their internal rules related to responsible lending.

On-site inspections performed in 2 credit institutions examined whether these banks assessed the suitability of relevant financial products for clients who had concluded an investment deposit contract. These inspections revealed no deficiencies.

An inspection of depositary services was performed in one credit institution. The FSA assessed whether the design of this area complied with legal requirements. As a result of this inspection the relevant credit institution was requested to complement the respective internal rules.

In 2014, an on-site inspection covering the area of securities market was performed in one credit institution where the handling of transaction orders as well as the registration and storage of data were examined. This inspection discovered deficiencies in the registration of transaction data, the storage of initial transaction orders, and the practice of and internal rules on the handling of transaction orders.

Insurance companies

In 2014, the economic environment was characterized by low interest rates that influenced life insurers the most. Activities of non-life insurers were driven by the increasing competition that was caused by the branches of EU insurers who found the Estonian market to be attractive for them.

Insurers were subjected to stress testing that was performed under the leadership of the European Insurance and Occupational Pensions Authority (EIOPA) and in active cooperation with financial supervisors of all EU countries. This stress test was aimed at evaluating the resilience of insurers to changes in financial markets and insurance risks. Three insurers from Estonia participated in this test. The results confirmed that life insurers with long-term commitments are more exposed to risks in Estonia due to continuously low interest rates.

As usual, the FSA analysed the tests of business continuity plans of all insurers in 2014 and their results, in order to assess whether the time and content of these tests complied with initial plans and whether the scope and results of the tests were in compliance with the priority of tested functions, processes and technical solutions. The FSA concluded that the testing of insurers' business continuity was free from material deficiencies.

In 2014, the FSA conducted besides other supervisory activities also on-site inspections in 2 branches of insurers.

The FSA focused on the issues related to the conclusion of insurance contracts, primarily the procedures related to loss adjustment and indemnification.

On-site inspections covered the following areas:

- Procedures related to the conclusion of insurance contracts and indemnification of losses;
- Presentation of mandatory information to policyholders.

As a result of these inspections, the FSA requested the relevant insurers to complement their internal rules. In addition, the FSA forwarded the results of its inspections to home financial supervision authorities of these insurers.

Insurance intermediaries

In the supervision of insurance intermediaries, the FSA focused on examining whether the interests of clients were protected.

In 2014, the FSA conducted besides other supervisory activities also on-site inspections in 2 insurance brokers and 1 insurance agent.

These on-site inspections covered the following areas:

- Compliance with the requirements related to the intermediation of insurance contracts.

On-site inspections performed in 2 insurance brokers examined the compliance with respective legal requirements, especially whether brokers perform their obligation to proceed from the interests of policyholders, identify insurable interest, make the best offer and disclose the amount of brokerage fee to the clients. As a result of these inspections, the FSA requested the relevant insurance brokers to comply with legal requirements and amend their internal rules.



Investment and pension funds

On the basis of reports submitted by fund managers on a monthly basis, the FSA examines whether the investments of investment and pension funds are in compliance with restrictions provided by legislation and fund's terms and conditions.

The FSA performs also quarterly risk-based analyses covering the financial situation of fund management companies, in order to monitor their profitability and meeting of prudential norms. In addition to regular report submitted to financial supervisors, the FSA presented ad-hoc inquiries to fund management companies in 2014 in order to obtain an overview of the management of operational risk as well as the nature and level of effects of the Russian-Ukrainian conflict on the activities of fund management companies. Results of these analyses showed that fund management companies had no direct significant risks related to this geopolitical conflict.

Requirements to own funds of fund management companies were strengthened in 2014 and they became significantly more complicated. Therefore, the FSA focused its attention on monitoring the capital adequacy of fund management companies. Fund management companies had not been subjected to risk-based capital requirements before 2014. However, the legislative amendment that entered into force in 2014 provides that persons who have obtained the alternative investment fund manager's license shall provide additional own funds for covering liability risks arising from professional negligence.

In 2014, the FSA conducted besides other supervisory activities also on-site inspections in 13 fund management companies.

These on-site inspections covered the following areas:

- Remuneration of managers of fund management companies;
- Expenses made and fees paid at the expense of mandatory pension funds;
- Compliance of investments of conservative pension funds with restrictions provided by law.

In 2014, the FSA examined in 5 fund management companies that managed mandatory pension funds the expenses made and fees paid at the expense of mandatory pension funds. In 6 fund management companies it examined the compliance of investments made by conservative pension funds with restrictions provided by law. On-site inspections in 2 fund management companies were aimed at examining the issues related to the remuneration of managers of fund management companies. The FSA identified no major deviations from law or other applicable requirements.

Investment firms

Annual Supervisory Review and Evaluation Process (SREP) in respect of financial and operational risks of investment firms is an important supervisory instrument in the area of investment firms. As an average, the capital requirements calculated for investment firms on the basis of SREP 2014 were 1.93 times higher than solvency margin requirements provided by law. This clearly shows that investment firms were exposed to high risks in 2014 and shall thus have bigger capital buffers to cover all risks.

The supervision of investment firms was focused on the assessment of risks arising from the conflict between Russia and Ukraine. Due to the volatility of financial markets, the FSA monitored the profitability of investments firms, geographical distribution of its assets and types of financial instruments used in case of clients' assets. In addition, the FSA examined changes in risk exposures and the effect of uncommon situations on the financial status of investment firms.

As sharp changes in capitalization level, unexpected losses, deteriorating financial status of owners and large exposures in Russian markets were major challenges for investment firms in 2014, the FSA required the submission of an action plan for risk mitigation from 2 investment firms, the submission of reporting on a more frequent basis from one investment firm and the maintenance of a bigger liquidity buffer from another investment firm.

The FSA performed no on-site inspections in investment firms in 2014. However, it monitored whether and how the investments firms eliminated deficiencies that had been identified during on-site inspections in 2013.

Payment institutions

In 2014, the supervision of payment institutions was primarily focused on the activities of major payment institutions in the anti-money laundering area. The FSA monitored the client base of payment institutions, especially focusing on transactions made by non-resident clients that showed large cash flows. In order to analyse the client base of payment institutions, the FSA assessed background documents of selected clients, asked for clarifications from the managers of payment institutions and examined the client data base of payment institutions.

As several payment institutions have failed to achieve an adequate business volume in order to ensure their profitability, the FSA examined whether payment institutions have complied with prudential norms. It had to intervene in various cases in 2014, and require from some payment institutions the submission of reporting on a more frequent basis, the presentation of a capitalization plan or the inclusion of additional own funds.

In addition, the FSA evaluates the compliance of managers with legal requirements. It discovered in one occasion in 2014 that the manager of a payment institution failed to meet the fit & proper criteria, and ordered the removal of the manager.

The FSA performed no on-site inspections in payment institutions in 2014. However, it monitored whether and how the payment institutions dealt with violations that had been discovered during on-site inspections in 2013 in the area of money laundering. In one occasion it ordered the supervised entity to align its activities with legislation.

Securities market

The FSA continued to guard the fairness of the securities market also in the environment of decreasing trading volumes – monitoring of daily transactions on the securities market led to the discovery of dozens of individual transactions that were suspected of market manipulation.

In 2014, the FSA filed a criminal complaint with the Prosecutor's Office in order to initiate a criminal proceeding against a private person and two companies on the grounds of market manipulation. Factual circumstances revealed a manipulative trading: the complaint was mainly based on wash sale transactions and the manipulation with closing price.

In order to identify the incidents of cross-border market abuse, the FSA worked in close collaboration with its main international cooperation partners – securities market supervisors from Latvia, Lithuania, United States, Bulgaria and Luxembourg.

The FSA published 334 warnings on its website regarding the persons who have provided investment services in Estonia or other EU countries without having the respective license.

Criminal complaints were filed against 3 persons for providing investment services without authorization.

The FSA supervises the reporting quality, reliability and comparability of issuers whose shares have been listed for trading on the regulated securities market operated by NASDAQ OMX Tallinn Stock Exchange. In 2014, it examined interim financial reports of 8 issuers and annual reports of 10 issuers.

In all cases it examined the correctness of calculations of earnings per share as published in annual reports as well as the correctness of profit distribution proposals. In addition, the FSA examined whether the issuers have disclosed their failure to comply with loan conditions and information on the estimation of goodwill and the fair value of assets. It discovered no material non-conformities in issuers' reporting.

As far as the activities of the operator of the regulated market are concerned, the surveillance was focused on corporate governance issues in 2014, including organisational issues related to technical solutions and their management in Baltic stock exchanges. Furthermore, the analysis covered the question whether and to what extent the statistical data on the Estonian regulated market is available to foreign investors and analysts. The adequacy of the capitalization level of the Stock Exchange and the registrar of the Estonian Central Register of Securities was also examined.

Finally, the FSA examined whether the activities of the company AS Eesti Väärtpaberikeskus were in compliance with the principles³ issued by CPSS-IOSCO in 2012.

3 These principles can be accessed through the press release published on the BIS website.

3.4. Transparency of financial services and consumer policy

3.4.1. Transparency of financial services

Pursuant to the Financial Supervision Authority Act, the FSA is not competent to settle the complaints submitted by the clients of financial services. The FSA is thus not able to issue mandatory precepts for parties to a specific civil dispute. However, it can render an independent opinion on the situation.

By registering and systematising the complaints, the FSA becomes aware of main disputable issues on financial services market and this contributes to the implementation of the risk-based supervisory model.

While the number of client complaints had demonstrated a constant increase since 2006, achieving the peak of 181 complaints in 2010, the period from 2011 to 2013 witnessed a decreasing trend in the number of complaints.

In 2014, the FSA received 108 complaints from clients in respect of financial services.

The majority of complaints concerned banking and insurance services, but a few complaints submitted concerned also investment services. The share of insurance disputes in the total number of complaints remained on the same level as in 2013; however, the share of banking disputes has somewhat increased.

In case of banking services, the majority of complaints concerned the problems occurred in making everyday banking transactions.

Number of complaints

	2006	2007	2008	2009	2010	2011	2012	2013	2014
Banks	36	24	95	97	88	101	80	64	72
Insurance	30	56	54	55	89	45	34	33	33
Others	6	2	4	5	4	2	5	5	3
TOTAL	72	82	153	167	181	148	119	102	108

Number of complaints by areas of service

	No of complaints
Settlements	27
Loan/credit	26
Property insurance	10
Motor TPL insurance	10
Payment service	8
Investment service	5
Land vehicles insurance	5
Others	5
Pension insurance	4
Life insurance	3
Accident insurance	2
Travel insurance	2
Deposit insurance	1

As far as lending services were concerned, clients complained the most about issues related to increased interest margin and the performance of contractual obligations. Clients of investment services complained about contract conditions. Clients of insurance services were mostly discontented with the activities of insurers in handling loss events, including with the level of compensation and refusals to pay the compensation.

Number of complaints by areas of service providers

	No of complaints	Market share in the sector ⁴
Swedbank AS	25	40%
Nordea Bank AB Estonian Branch	15	14%
AS SEB Pank	14	23%
If P&C Insurance AS	8	26%
Danske Bank A/S Estonian Branch	7	10%
Codan Forsikring A/S Estonian Branch	5	11%
AAS Gjensidige Baltic Estonian Branch	4	2%
Swedbank P&C Insurance AS	4	16%
AS DNB Pank	3	3%
ERGO Insurance SE	3	17%
AS Eesti Krediitipank	3	1%
BTA Insurance Company SE Estonian Branch	3	4%
AS LHV Pank	2	3%
Admiral Markets AS	2	34%
AAS "Baltikums"	1	NA
BIGBANK AS	1	2%
AS Citadele banka Estonian Branch	1	1%
ERGO Life Insurance SE Estonian Branch	1	6%
Mandatum Life Insurance Baltic SE	1	13%
Seesam Insurance AS	1	10%
Swedbank Life Insurance SE	1	39%
UAB DK "PZU Lietuva" Estonian Branch	1	4%
Versobank AS	1	1%
Western Union Payment Services Ireland Ltd	1	NA

⁴ Comment: market shares as at 31.12.2014. Market shares are based on insurance premiums excluding reinsurance premiums (in insurance sector) or asset volumes (in case of banking sector, fund management companies and investment funds). Data is presented on solo basis and does not include any subsidiaries, affiliates or branches.

3.4.2. Promotion of public awareness

Besides its supervisory activities, the FSA provides objective information on financial services and products to the clients of financial services.

It is important for the clients of financial services to be an equal party to a contract and to be able to consider also the aspects undisclosed by service providers when choosing the service, concluding and performing contracts or protecting their interests.

In December 2014, the FSA commissioned a survey from Turu-uuringute AS on the use of financial services and the awareness of customers, in order to ensure a better planning of consumer information in future. According to this survey, customers of financial services would like to receive additional information on investment deposits, housing loans and the purchase and sale of securities on the stock exchange. Also, they would like to receive more information on the possibilities to amend or prematurely terminate various contracts concluded with credit institutions as well as on relevant consequences. In addition, consumers considered it essential to receive information on the actual price and cost of services. In the area of insurance services, customers would like to be informed of the cases where losses are not to be compensated and of risks that are covered by property insurance.

This survey demonstrated that Estonian citizens are not very interested in using financial services. 48% of respondents were not interested in receiving any additional information on the area of financial services, and 72% of respondents had no plans to use any financial services during the next year. Although 44% of respondents considered themselves to be "more of a saving type", only a third of respondents were aware of such saving and investment methods where the funds of clients were protected by the state.

The FSA reorganised the area of consumer information in 2014, and started to focus on supporting the forwarding on necessary messages in the area of business conduct supervision.

3.5. Development of regulative environment

3.5.1. Legislative drafting

Year 2014 was characterized by significant volumes of legislative drafting in the financial sector area – both material amendments to existing legislation and drafting of completely new legislation. The FSA contributed to legislative drafting, within the limits of its powers and capacities, by presenting opinions to working parties that prepared the relevant draft acts and by participating in the work of these working parties.

The FSA was engaged in four major legislative projects in 2014:

- Financial Crisis Prevention and Resolution Act (FCPRA). FCPRA is based on the Directive 2014/59/EU of the European Parliament and of the Council and is primarily applicable to credit institutions. FCPRA provides measures that would be most efficient for the prevention of financial crisis or would allow the resolution of financial crisis at minimal cost. The Financial Supervision Authority would be the national resolution authority.
- Credit Providers and Intermediaries Act (CPIA). CPIA is aimed at harmonizing the requirements applicable to financial institutions, increasing the liability of credit providers and intermediaries for the performance of requirements related to their activities, and gaining a picture of the scope of their activities on Estonian markets.

CPIA provides requirements applicable to the activities of credit providers and intermediaries, and introduces the obligation to apply for a respective license. CPIA brings additional credit providers and intermediaries under the FSA's supervision in addition to previously supervised credit institutions. CPIA is related to the Directive 2014/17/EU of the European Parliament and of the Council.

- Insurance Activities Act (IAA). The new IAA is aimed at regulating insurance activities and insurance mediation area, complementing and updating the existing insurance and intermediation regulations. The updating of regulations in the area of insurance was a EU-wide initiative. IAA insures that national legislation is in compliance with new EU requirements that are provided by the following insurance-related Directives: Directives 2009/138/EC and 2014/51/EU of the European Parliament and of the Council.
- Investment Funds Act (IFA). IFA is aimed at enabling the establishment of new fund structures and expanding thus the possibilities of investors to make investments through investment funds. The draft act is related to the following EU legislation: Directives 2003/41/EC, 2007/44/EC, 2009/65/EC, 2011/61/EU and 2013/14/EU of the European Parliament and of the Council and Commission Directives 2007/16/EC and 2010/44/EU.

3.5.2. Litigation

The FSA was involved in 12 judicial proceedings, 3 of which were concluded in 2014.

The first case concerned a complaint submitted by certain shareholders of a credit institution who asked the court to invalidate the qualifying holding authorization that the FSA had issued to other shareholders of the same credit institution. The court rejected their complaint and concluded that independent public financial supervision was performed in public interest.

The second case concerned a negative decision adopted by the FSA regarding the inclusion of an insurance intermediary to the list of insurance intermediaries. The FSA had concluded that the professional or business reputation of

a Board member of this insurance intermediary failed to meet the fit&proper criteria. This dispute continued through all judicial stages. The Supreme Court upheld the administrative decision of the FSA.

The third case that concerned the Comprehensive Assessment of banks' assets was terminated by the complainant who withdrew the complaint.

A court action that was initiated against the FSA by an issuer traded on the stock exchange in order to challenge the FSA's decision of 16 December 2011 (on a misdemeanour regarding the violation of inside information disclosure requirements) was concluded in 2014 because of the expiry of this misdemeanour episode.

3.5.3. Development of reporting

Regulation (EU) No 575/2013 of the European Parliament and of the Council on prudential requirements entered into force on 1 January 2014. This Regulation provides common supervisory reporting requirements to all investment firms and credit institutions operating in the European Union. These requirements were established by the Commission Implementing Regulation (EU) No 680/2014 that became effective on 1 January 2014. Established reporting standards harmonized the content, format, reporting periods and submission deadlines of supervisory reports of EU credit institutions and investment firms.

Among the reporting forms to be submitted under the new harmonized EU reporting standards, 49 concern the calculation and monitoring of prudential requirements and 65 concern the consolidated financial status.

In 2014, in relation to the preparatory efforts made for the implementation of the new risk-based capital adequacy framework for life and non-life insurers – Solvency II – the FSA focused on the EIOPA Guidelines on Submission of Information to National Competent Authorities. These Guidelines provide guidance for insurers and reinsurers and their consolidation groups for the submission of reporting before the application of Solvency II requirements on 1 January 2016.

Extensive new requirements will be a challenge for both market participants and the FSA.

3.5.4. Guidelines issued by the Financial Supervision Authority

The Financial Supervision Authority explains in its Advisory Guidelines various legislative provisions that regulate the financial sector and directs the activities of supervised entities so that they comply with legislative requirements.

The establishment of European Single Supervisory Mechanism (SSM) and participation in the network of European financial supervision authorities mean that various national supervisory practices and regulative frameworks will be harmonized. This is reflected by the increased number of documents that have been transposed into Estonian law and enacted as the FSA's advisory guidelines.

In 2014, the FSA transposed and enacted as its advisory guidelines the following guidelines issued by European financial supervision authorities:

- Guidelines on the model MoU concerning consultation, cooperation and the exchange of information related to the supervision of AIFMD entities (ESMA/2013/998);
- Guidelines on retail deposits subject to different outflows for purposes of liquidity reporting under Regulation (EU) No 575/2013, on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (Capital Requirements Regulation – CRR) (EBA/GL/2013/01);
- Guidelines on ETFs and other UCITS issues (ESMA/2014/937);
- Guidelines and Recommendations regarding the implementation of the CPSS-IOSCO Principles for Financial Market Infrastructures in respect of Central Counterparties (ESMA/2014/1133);
- Guidelines on reporting obligations under Articles 3 and 24(1), (2) and (4) of the AIFMD (ESMA/2014/869);
- Guidelines on disclosure of encumbered and unencumbered assets (EBA/GL/2014/03);
- Guidelines on harmonised definitions and templates for funding plans of credit institutions under Recommendation A4 of ESRB/2012/2 (EBA/GL/2014/04).

Several EIOPA guidelines that were enacted as the FSA's advisory guidelines and clarified the transition to Solvency II became effective in 2014:

- Guidelines on Pre-application for Internal Models (EIOPA-CP-13/011). These Guidelines are aimed at clarifying various pre-application-related issues to insurers who are planning to use internal models for the calculation of their capital needs from 2016 onwards;
- Guidelines on the System of Governance (EIOPA-CP-13/08) clarify how fit&proper requirements for key persons, risk management, the principle of reasonable investments, own funds, internal control system and key functions are linked with the whole system of governance;
- Guidelines on Forward Looking Assessment of Own Risks (based on the ORSA principles) (EIOPA-CP-13/09) clarify the nature, principles and scope of the assessment of own risks in the preparatory phase of Solvency II.

3.6. International cooperation

3.6.1. Common banking supervision in the euro area

European Single Supervisory Mechanism SSM consisting of the European Central Bank and euro-area national banking supervisory authorities became fully functional from 4 November 2014. Its task is to ensure the safety and reliability of the European banking system, enhance financial integration and stability and guarantee the consistency of supervision.

SSM together with the Single Resolution Mechanism are the two main pillars of the European Banking Union. All euro-area countries are participating in the SSM.

SSM does not include the supervision of financial services and anti-money laundering or the prudential supervision of other financial intermediaries. Credit institutions are classified as significant institutions and less significant institutions under the Council Regulation (EU) No 1024/2014.

The European Central Bank (ECB) performs direct supervision over 123 significant banking groups in the euro-area. Among the credit institutions operating in Estonia, Swedbank AS and AS SEB Bank are subjected to the ECB's direct supervision. Direct supervision means that the decisions are made by the Supervisory Board of the SSM, and the activities are planned and executed by the ECB in cooperation with the FSA who provides main resources for the supervision.

Other credit institutions operating in Estonia are still subjected to the FSA's direct supervision. The FSA follows general instructions, if any, given by the ECB.

Besides ensuring the compliance of 123 euro-area banks with capital and liquidity requirements, the tasks of the ECB include, since putting in place a system of common bank supervision, also the authorisation of credit institutions and the withdrawing of authorisations of credit institutions and the approval of qualifying holding acquisitions in banks.

Supervisory activities in respect of significant banks are performed by Joint Supervisory Teams (JSTs) that consist of ECB's experts and national supervisors of the relevant bank.

SSM's key decision-making body is the Supervisory Board. Its decisions are approved by the ECB's Governing Council. The Supervisory Board consists of the representatives of ECB and national financial supervision authorities of euro-area. Mr Kilvar Kessler, Chairman of the FSA's Management Board, is the member of the Supervisory Board, and his alternate is Mr Andres Kurgpõld, Member of the FSA's Management Board.

The Supervisory Board held 22 meetings in Frankfurt and discussed 208 agenda items in 2014. It adopted 101 decisions by a written procedure in 2014.

As 2014 was above all a preparatory year for the common banking supervision, most of the decisions adopted before the introduction of common supervision on 4 November 2014 were aimed at making preparations for the single system.

In order to draw a comparative picture of the situation, the SSM together with the ECB performed the Comprehensive Assessment (CA) of euro-area banks. It consisted of the Asset Quality Review (AQR) and strength analysis. Asset Quality Review encompassed also the assessment of the actual value of banks' assets and the adequacy of collaterals as at 31 December 2013.

Besides participating in the work of the SSM's Supervisory Board, Mr Kilvar Kessler, Chairman of the FSA's Management Board, participated also in the work of the SSM's Steering Committee. The Steering Committee is a body consisting of 8 members, 3 of them from the ECB and 5 from national supervision authorities, based on rotation principle. Its task is to support the activities of the Supervisory Board and make preparations for its meetings.

Experts of the FSA were involved in 21 different working parties or committees in 2014 and participated in 68 meetings in total.



3.6.2. Participation in European financial supervision authorities

Estonia as an EU Member State is a part of the common financial services market and its financial stability depends directly on its cooperation with other EU Member States. Participation in the work of European financial supervision authorities is one of the possibilities to contribute to the development of EU supervisory policies.

Representatives of EU national supervision authorities participate in the Board of Supervisors of each European Supervision Authority (ESA) – the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA) and the European Securities and Markets Authority (ESMA).

The Joint Committee of the European Supervision Authorities addressed inter alia the budgets of the European Supervision Authorities and strategic issues as well as prepared surveys on financial market developments and risks.

In 2014, representatives of the FSA acted as members in 56 different committees or working parties and participated in 102 meetings of these committees or working parties.

European Banking Authority (EBA)

Mr Andres Kurgpõld, Member of the FSA's Management Board, is the voting member of the EBA's Board of Supervisors, and Mr Kilvar Kessler, Chairman of the FSA's Management Board, is the alternate member. Mr Ander Kurgpõld was nominated by the EBA as an alternative member of EBA's committee for the resolution of disputes between its members.

Representative of the FSA participated in 7 meetings of the EBA's Board of Supervisors in 2014.

Development of various implementing measures related to the Bank Recovery and Resolution Directive (BRRD) became one of the main issues for the EBA from the end of 2014 onwards.

In 2014, the activities of EBA were mainly focused on the development of timetable and method for stress testing organised together with the European Central Bank. EBA approved 11 guidelines in 2014.

In 2014, experts of the FSA participated in the work of 3 standing committees and sub-groups of the EBA, in total in 24 meetings.

European Insurance and Occupational Pensions Authority (EIOPA)

Mr Kilvar Kessler, Chairman of the FSA's Management Board, is the voting member of the EIOPA's Board of Supervisors, and Mr Andres Kurgpõld, Member of the FSA's Management Board, is the alternate member.

Representative of the FSA participated in 7 meetings of the EIOPA's Board of Supervisors in 2014.

One of the major events in 2014 was the performance of stress testing by EIOPA. Results of the stress testing were published in November 2014. EIOPA approved 2 guidelines in 2014.

In 2014, experts of the FSA participated in the work of 6 committees and working groups of the EIOPA, in total in 30 meetings.

European Securities and Markets Authority (ESMA)

Mr Andre Nõmm, Member of the FSA's Management Board, is the voting member of the ESMA's Board of Supervisors, and Mr Kilvar Kessler, Chairman of the FSA's Management Board, is the alternate member.

Representative of the FSA participated in 8 meetings of the ESMA's Board of Supervisors in 2014.

In 2014, ESMA continued to focus primarily on the issues related to the following instruments: Markets in Financial Instruments Directive (MiFID II), Market Abuse Directive (MAD), Market Abuse Regulation (MAR) and European Market Infrastructure Regulation (EMIR).

The establishment of common European IT-systems was considered under the framework of MiFID II/MiFIR and EMIR implementation for the first time and relevant discussions included the issue whether the Member States would have to develop market infrastructure systems:

- MiFIR Instruments Reference Data;
- MiFIR Transaction Reporting Project;
- Single Access Point for Querying Trade Repositories.

Estonia decided to participate in the development project of Single Access Point for Querying Trade Repositories.

ESMA approved 2 guidelines in 2014.

In 2014, experts of the FSA participated in the work of 8 committees and working groups of the ESMA, in total in 45 meetings.

The FSA became a party to the ESMA's cooperation agreement that was signed in 2014 when ESMA finalised supervisory cooperation agreements for alternative investment funds under the AIFMD with relevant supervision authorities from Egypt, New Zealand, Vietnam and South Korea. Furthermore, the FSA signed the ESMA's cooperation agreement for supervisory activities and exchange of information that encompassed all EU and EMP members.

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

In September 2014, Estonia was successful in defending the Assessment Report on Anti-Money Laundering and Combating the Financing of Terrorism at the Plenary Meeting of the Council of Europe's anti-money laundering body MONEYVAL⁵. This Report stated that the performance of due diligence measures for anti-money laundering and prevention of terrorist financing by entities supervised by the FSA were largely in compliance with international standards and that obligated persons were subjected to efficient supervision in Estonia.

Furthermore, the report emphasised some areas where the assessors felt that Estonia should take some steps towards enhancing the efficiency of anti-money laundering and prevention of terrorist financing. It stated that the penalties applied by the FSA for identified violations were insufficient in monetary terms. In addition, the report stated that in case of certain supervised entities more attention should be turned to actual beneficiaries in business relations and to the identification of the origin of assets used in transactions.

The report addressed also the risk-based supervisory model applied by the FSA. The assessors considered that despite of the rationale for implemented principles and measures, the FSA should increase its supervisory activities in life insurance sector in the area of anti-money laundering and prevention of terrorist financing.

The FSA takes the findings of the MONEYVAL report into account in its activities.

Together with other Estonian competent authorities the FSA prepared an assessment of threats related to money laundering and terrorist financing. It was submitted for approval to the Government Committee on Anti-Money Laundering. The national threat assessment was based on the methodology of the World Bank. It considered that Estonian credit and financial institutions were highly prepared to comply with anti-money laundering standards and due diligence measures and that implemented supervisory and control systems were efficient.

5 <http://www.coe.int/t/dghl/monitoring/moneyval/>

3.6.4. Cooperation with foreign supervisory authorities

The FSA continued its cooperation with national supervision authorities of EU Member States in 2014 in order to gather detailed information from home supervisors of parents of supervised entities in Estonia. This supervisory cooperation was important for the harmonisation of supervisory priorities, especially in the supervision of cross-border groups and within the framework of common banking supervision.

The FSA-led joint meeting between Management Boards of the FSA and the Latvian Financial Supervision Authority⁶ and the Governing Council of the Lithuanian Central Bank was organised in March in Riga. This meeting addressed major supervisory priorities and covered the developments in the financial sector. Similar meetings were also organised with managements of Finnish and Sweden supervision authorities.

European Central Bank became a party to the banking cooperation framework in 2014 – as a consequence, respective amendments were made into cooperation agreements

and the composition of supervisory colleges was changed. The FSA participates as an observer in supervisory colleges of significant banks.

Representatives of the FSA participated in the work of 6 supervisory colleges – the supervisory colleges for Swedbank Group, SEB Group, DNB Group, Danske Group, Nordea Group and Citadele Group.

Pursuant to the Directive 98/78/EC on the supplementary supervision of insurance groups, the FSA was also involved in cooperation with other national supervision authorities on supplementary supervision of insurance groups. In 2014, 7 of the insurers supervised by the FSA – SEB Elu- ja Pensionikindlustus, Compensa Life Vienna Insurance Group SE, Mandatum Life Insurance Baltic SE, D.A.S. Õigusabikulude Kindlustuse AS, ERGO Insurance SE, If P&C Insurance AS and Seesam Insurance AS – as well as the fund management company Nordea Pensions Estonia AS belonged into insurance groups that were subject to supplementary supervision.

3.6.5. Cooperation with other international organisations

Together with the Eesti Pank, the FSA continued to participate in the work of the European Systemic Risk Board (ESRB) under the auspices of the European Central Bank. The FSA participates in meetings of the General Board of ESRB as a member without voting rights.

In 2014, the FSA participated in 4 General Board meetings that discussed issues related to the financial stability.

In addition, the FSA participated as a member in the work of following global organisations in 2014: International Association of Insurance Supervisors (IAIS), Bank of International Settlements (BIS), including the Group of Banking Supervisors from Central and Eastern Europe (BSCEE), International Organisation of Securities Commission (IOSCO) and the

Organisation for Economic Cooperation and Development (OECD).

During the evaluation visit by the OECD, the FSA presented a review to the OECD on the implementation of post-accession recommendations.

The FSA contributed to the evaluation visits of rating agencies Standard & Poor's and Fitch Ratings in 2014. In addition, the FSA presented reviews on developments in and major financial indicators of the Estonian financial sector during the IMF's Article IV Mission. During the brief visit organised by the IMF in November, the FSA informed the new mission head on financial sector developments related to the introduction of SSM.

4 Financial Supervision Authority's 2014 Annual Report of Revenues and Expenditures



Accounting policies

General

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

Transactions in foreign currency

Foreign currency includes all currencies other than euro (i.e. accounting currency of the FSA). Reporting of any foreign currency transaction is based on the official exchange rate of the European Central Bank on the day of the transaction.

Operating lease

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

REVENUE AND EXPENDITURE ACCOUNT

(In thousands of EUR)

	ANNEX	2014	2013
REVENUE			
Supervisory fees	1	7,843	4,587
Other revenue	2	22	22
Total operational revenue		7,865	4,609
EXPENDITURE			
Personnel expenditure	3	2,942	2,958
Misc. operational expenditure	4	2,551	1,394
Other expenditure	5	58	45
Total operational expenditure		5,551	4,397
Profit for core activities		2,314	212
Financial income and expenditure	6	-3	0
Profit for the accounting year		2,311	212

ANNEXES TO THE ANNUAL REPORT OF REVENUES AND EXPENDITURES

ANNEX 1

Supervisory fees (In thousands of EUR)		
	2014	2013
Credit institutions	5,920	2,922
Non-life insurers	686	570
Fund management companies	394	344
Life insurers	375	335
Investment firms	175	152
Insurance brokers	154	138
Payment institutions	110	99
Registrar of Central Register of Securities Operator of regulated securities market	29	27
Total	7,843	4,587

**Supervisory fee shares calculated on the basis of
assets (%)**

	2014	2013
Credit institutions	0.0288	0.0133
Non-life insurers	0.097	0.095
Fund management companies	0.007/ 0.013	0.006/ 0.012
Life insurers	0.023	0.02
Investment firms	0.23	0.18
Insurance brokers	0.92	0.9
Payment institutions	0.22	0.2
Registrar of Central Register of Securities Operator of regulated securities market	0.5	0.4

The financing principles of the Financial Supervision Authority are provided in the Financial Supervision Authority Act that is available on the FSA website on the following address: www.fi.ee.

As to the supervisory fee of fund management companies, different shares calculated on the basis of assets are applied to different types of funds.

Supervisory fees consist of two shares: firstly, the capital share, which is the amount that equals one percent of the total of the minimum (net) own funds, equity or share capital of the supervised entity; secondly, the share calculated on the basis of assets, which is the amount that equals the percentage of the supervised entity's assets, total amount of insurance payments, calculated assets or commission fees established by the Minister of Finance at the proposal of the Supervisory Board of the FSA.

Pre-payments of the capital share and the share calculated on the basis of assets are made to the FSA by 31 December of the year preceding the financial year.

The final payment is made by 1 September of the financial year.

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

ANNEX 2

Other revenue (In thousands of EUR)		
	2014	2013
Processing fees	13	10
Other revenue	9	12
Total	22	22

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

The item *Other revenue* shows the amount paid to the FSA by a former employee pursuant to the mutual internship agreement.

ANNEX 3

Personnel expenditure (In thousands of EUR)		
	2014	2013
Salaries	2,158	2,172
Taxes	741	748
Supervisory Board's compensations	43	38
Total	2,942	2,958

Salary expenditures include salary expenditures together with bonuses, compensations for members of the Management Board and the increase in the estimated vacation liability for the unused vacation of the FSA's employees (including social taxes) amounting to € 12,000.

At the end of 2014, the average salary of an employee of the FSA amounted to € 2,253 euro. Bases for the calculation of average salary have been amended and the FSA follows the guidance of the Statistics Estonia for the calculation of average salary. The FSA's salary fund for 2014 increased by 5% in comparison with 2013.

In 2014, the total sum of compensation paid to the Supervisory Board and Management Board members amounted to € 275,000 (€ 365,000 in 2013). Total bonuses paid to employees accounted for 7,8% of salary expenditures.

The number of employees totalled 72 as at 31.12.2014 (including members of the Management Board).

ANNEX 4

Misc. operational expenditure (In thousands of EUR)		
	2014	2013
Membership fees of international organisations	519	405
Real estate lease	300	285
IT infrastructure, software and development	327	203
Business trips	244	194
Office expenses	70	85
Communication expenses	33	84
Training expenses	53	54
Accounting expenses	52	50
Legal assistance and consultation	933	10
Expenses for information agencies	9	8
Personnel work	4	8
Lease for fixed assets	3	4
Auditing expenses	4	4
Total	2,551	1,394

Operational expenditure

The item *Membership fees* includes membership fees paid by the FSA to the following international organisations: ESMA, EIOPA, EBA, IAIS, BSCEE, IOSCO and OECD.

The item *Real estate lease* includes the office space leased from the Eesti Pank with a total area of 1,396 m² at a price of € 17.93 per m² each month, which includes all costs related to the administration of the office space.

The item *IT infrastructure, software and development* includes IT services bought from the Eesti Pank at an estimated value of € 3,561 per user as well as the FSA's IT infrastructure and development projects.

The item *Business trips* includes all trips related to representing the FSA and supervisory cooperation. Business trips were primarily related to ECB/SSM and ESA committee and sub-committee meetings and bilateral meetings with other supervisory authorities. In total, there were 337 business trips in 2014 (263 in 2013). Significant increase in the number of business trips was caused by the implementation of and participation in the European Single Supervisory Mechanism.

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

The item *Communication expenses* includes the cost of the FSA's consumer education program and the website www.minuraha.ee, and the expenses for publishing information materials for consumers and the FSA Yearbook.

The item *Training expenses* includes the expenses for training locally and abroad, including travel expenses. In 2014, the average cost for training abroad (together with travel expenses) was € 1,079 and for local training € 251 (€ 997 and € 236 respectively in 2013).

Training was mostly provided in the following areas: development of prudential regulation in banking and insurance sectors, central bank and financial sector, securities market services and developments.

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

The item *Legal assistance and consultation* shows expenditures incurred due to FSA's expenses in legal proceedings, the involvement of experts, special audits and legal opinions related to the supervisory activities of the FSA. Significant increase in the expenses for legal assistance and consultation in comparison with 2013 was caused by the performance of Comprehensive Assessment within the framework of SSM, including the performance of Asset Quality Review.

The item *Expenses for information agencies* includes the user fee for information agencies and the cost of the FSA's website.

The item *Personnel work* includes recruitment costs for the employees of the FSA.

The item *Lease for fixed assets* includes the lease paid by the Financial Supervision Authority to the Eesti Pank. The lease for fixed assets used by the Financial Supervision Authority, including IT hardware and software as well as inventory, is paid per year. The amount of the lease is equal to the depreciation rate at the Eesti Pank for the specific fixed assets.

The item *Auditing expenses* includes the expenses of auditing the Report of Revenues and Expenses of the FSA. According to Article 51(3) of the Financial Supervision Authority Act, the report is audited by an auditor of the Eesti Pank.

ANNEX 5

Other expenditure (In thousands of EUR)

	2014	2013
Compensation and benefits	30	22
Cultural events and sports	23	23
Legal expenses	5	0
Total	58	45

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

The item *Culture and sports* reflects the expenditures for events organised for the employees of the FSA.

The item *Legal expenses* reflects potential expenses related to court actions.

ANNEX 6

Financial income and expenditure (In thousands of EUR)

	2014	2013
Financial income and expenditure	-3	0
Total	-3	0

The FSA keeps its reserves in Eesti Pank. Interest rate paid by Eesti Pank during the period from 1 January 2013 to 30 September 2014 was based on the interest rate on the deposit facility set by the European Central Bank. Since 1 October 2014, Eesti Pank pays interests on the FSA's assets based on Eonia interest rate.

BALANCE SHEET (In thousands of EUR)

	31.12.2014	31.12.2013
ASSETS		
Cash and bank accounts	8,576	10,217
Supervisory fees receivable	1,843	923
Total assets	10,419	11,140
LIABILITIES AND RESERVE		
Payables to employees	99	87
Misc. payables	656	728
Deferred income	4,765	7,742
Reserve for future liabilities	5	0
Total liabilities	5,525	8,557
Reserve	2,583	2,371
Profit/loss for the accounting year	2,311	212
Total reserve and profit/loss for the accounting year	4,894	2,583
Total liabilities, reserve and profit for the accounting year	10,419	11,140

EXPLANATORY NOTES FOR THE 2014 BALANCE SHEET

The item *Cash and bank accounts* shows the balance of current accounts in the Eesti Pank.

The item *Supervisory fees receivable* shows prepayments of supervisory fees for 2015 not yet received by the FSA in the amount of € 1,843,000.

The item *Payables to employees* includes vacation liabilities. Vacation liabilities include the estimated vacation liability for vacation not taken by FSA employees in the amount of € 99,000.

The item *Misc. payables* includes expenditures by the FSA covered by the Eesti Pank in 2014, which the FSA will compensate to the Eesti Pank in 2015.

The expenses of the FSA are recorded in the annual report according to the accrual method.

The item *Deferred income* includes the prepayments of 2015 supervisory fees.

The item *Reserve for future liabilities* shows potential legal expenses related to on-going court actions.

Profit for 2013 within the amount of € 212,000 was transferred to the reserve pursuant to the Resolution of 21 March 2014 of the Supervisory Board of the FSA. The balance of the reserve totalled € 2,583,000 by year 2014.

The profit for the accounting year 2014 was € 2,311,000. Profit for 2014 was mostly caused by the fact that actual expenses for legal assistance and consultation decreased, and the difference was budgeted for the performance of Comprehensive Assessment within the framework of ECB/SSM, including the performance of Asset Quality Review.



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SÕLTUMATU VANDEAUDIITORI ARUANNE

Finantsinspektsiooni nõukogule:

Oleme auditeerinud Finantsinspektsiooni tulude-kulude aastaaruannet, mis koosneb bilansist seisuga 31. detsember 2014, antud kuupäeval lõppenud aruandeaasta kohta koostatud tulude-kulude aruandest, oluliste arvestuspõhimõtete kokkuvõttest ja muudest selgitavatest lisadest.

Juhatuse vastutus raamatupidamise aastaaruande koostamise eest

Juhatus vastutab nimetatud tulude-kulude aastaaruande koostamise ja õiglase esituse eest kooskõlas Finantsinspektsiooni seaduse ja tulude-kulude aruandes kirjeldatud arvestuspõhimõtete ning sellise sisekontrolli eest, nagu juhatus peab vajalikuks, et võimaldada kas pettusest või veast tulenevate oluliste väärkajastamisteta raamatupidamise aastaaruande koostamist.

Vandeaudiitori vastutus

Meie vastutame arvamuse eest, mida avaldame nimetatud raamatupidamise aastaaruande kohta meie auditi põhjal. Viisime oma auditi läbi kooskõlas rahvusvaheliste auditeerimisstandarditega (Eesti). Need standardid nõuavad, et me järgime eetikanõudeid ning planeerime ja viime auditi läbi saamaks põhjendatud kindlust asjaolule, et tulude-kulude aastaaruanne ei sisalda olulisi vigu.


Audit hõlmab protseduuride läbiviimist eesmärgiga saada tõendusmaterjali tulude-kulude aastaaruandes esitatud arvnäitajate ja avalikustatud informatsiooni kohta. Sooritatavad auditi protseduurid sõltuvad vandeaudiitori hinnangutest, sealhulgas hinnangust riskile, et tulude-kulude aastaaruanne võib sisaldada olulisi vigu, mis tulenevad pettusest või eksimusest. Nimetatud riski hindamisel, eesmärgiga planeerida asjakohaseid auditi protseduure, võtab vandeaudiitor arvesse tulude-kulude aastaaruande koostamiseks ja õiglase esitusviisi tagamiseks ettevõttes juurutatud sisekontrollisüsteemi, kuid ei anna hinnangut selle toimivuse kohta. Audit hõlmab ka kasutatud arvestuspõhimõtete asjakohasuse ja juhatuse poolt antud arvestushinnangute põhjendatuse ning tulude-kulude aastaaruande üldise esitusviisi hindamist.

Usume, et meie kogutud auditi tõendusmaterjal on piisav ja asjakohane arvamuse avaldamiseks.

Arvamus

Oleme seisukohal, et tulude-kulude aastaaruanne kajastab olulises osas õiglaselt Finantsinspektsiooni finantsseisundit seisuga 31. detsember 2014 ning aruandeaasta majandustulemust kooskõlas Finantsinspektsiooni seaduse ja tulude-kulude aruandes kirjeldatud arvestuspõhimõtetega.

20. märts 2015


Veiko Hintsov
Avaliku sektori vandeaudiitor nr 328
AS Deloitte Audit Eesti
Tegevusluba nr 27


Anne Mobel
Avaliku sektori vandeaudiitor nr 590

Deloitte tähistab ühte või mitut Deloitte Touche Tohmatsu't, mis on UK piiratud vastutusega äriühing ja selle liikmesfirmade võrgustikku, kus iga liikmesfirma on juridiliselt eraldiseisev ja sõltumatu ettevõtte. Deloitte Touche Tohmatsu ja tema liikmesfirmade juriidilise struktuuri detailset kirjeldust vaata www.deloitte.ee.

Deloitte Touche Tohmatsu Limited liige



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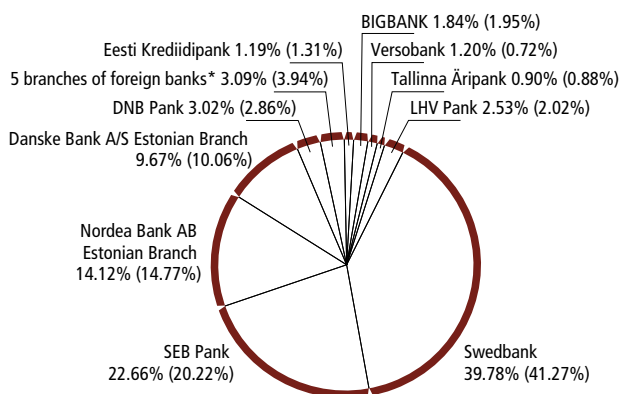
Overview of the financial market in Estonia

6.1. Credit institutions



As at 31 December 2014, there were 8 locally authorised credit institutions and 7 branches of foreign credit institutions operating in Estonia. The aggregate market share of 4 major banks by asset volumes – Swedbank AS, AS SEB Pank, Nordea Bank AB Estonian Branch and Danske Bank A/S Estonian Branch – totalled 86% (also 86% in 2013) (See Figure 1).

Figure 1. Market shares of banks based on asset volume, 31.12.2014
(in brackets 31.12.2013)



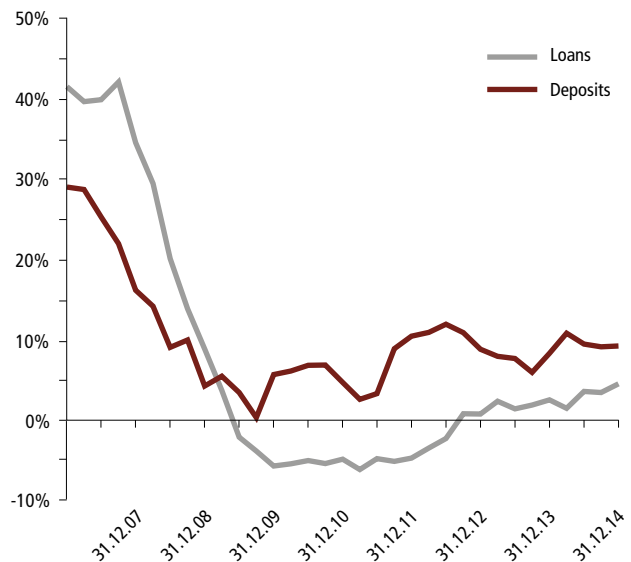
*(excl. Nordea and Danske)

5 branches of foreign banks: AS Citadele banka Estonian Branch, Scania Finans AB Estonian Branch, Folkia AS Estonian Branch, Svenska Handelsbanken AB Estonian Branch and Pohjola Bank plc Estonian Branch

Growth of loan portfolio

The aggregate loan portfolio of banking sector increased 4.5%. Activity in the lending business of banks somewhat picked up in 2014, especially in the area of corporate loans. Volume of deposits continued its growth as well, the annual increase being 9.2% (See Figure 2).

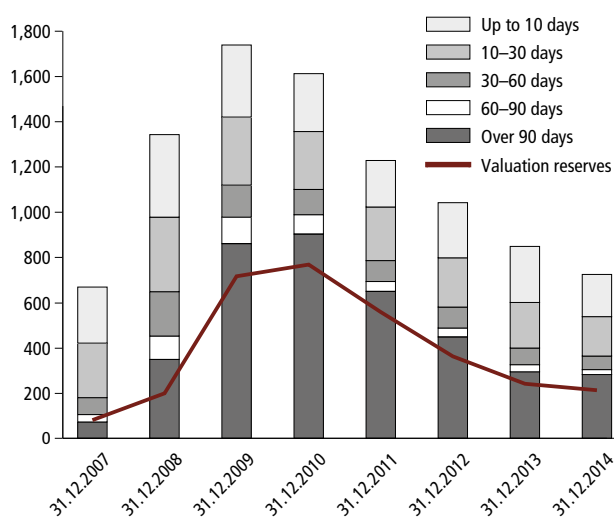
Figure 2. Annual growth in loans and deposits (%)



Quality of loan portfolio continued to improve

The total volume of overdue loans decreased in the end of 2014 as compared to 2013 (See Figure 3), both in absolute figures and as a share of the combined loan portfolio. At the end of 2014, loans overdue for more than 90 days accounted for 1.8% of the combined loan portfolio (2.0% in 2013). The coverage of long-term overdue loans with valuation reserves was still good: 75% of loans overdue for more than 90 days were covered by valuation reserves at the end of 2014 (82% in 2013).

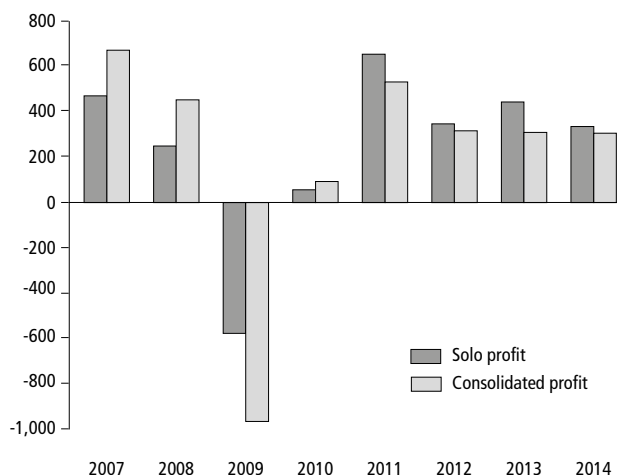
Figure 3. Loans overdue and valuation reserves of banks (in millions of EUR)



Good profits earned by banks

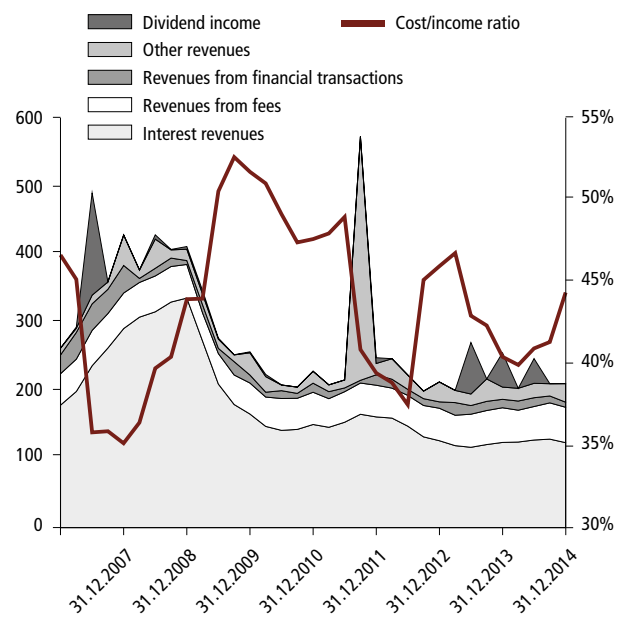
Annual profits earned by banks totalled € 337.3 million on solo basis and € 308 million on consolidated basis (€ 445.5 million and € 310,6 million respectively in 2013) (See Figure 4). Profits earned in 2014 remained on a lower level than in 2013: on solo basis 24% less and on consolidated basis 1% less than in the previous year.

Figure 4. Net profit (loss) of banks and banking groups (in millions of EUR)



Similarly to previous years, interest revenue from lending activities continued to form the main source of income for banks in 2014. Banks' incomes somewhat decreased compared to the previous year, primarily on the account of diminishing dividend income (See Figure 5). The second half of 2014 witnessed a volume increase in the loan portfolio leading to additional interest revenue that balanced the drop in interest revenue caused by the continuously low level of Euribor. Despite the increased cost, the cost to income ratio of the banking sector remained on an excellent level – 44.3% (40.4% in 2013).

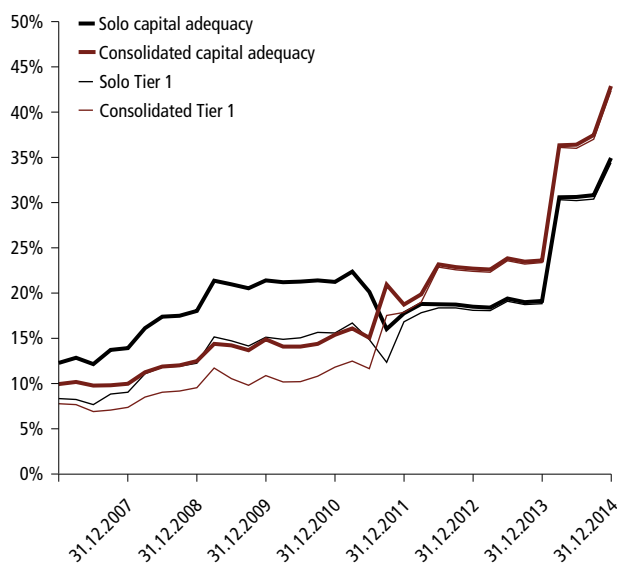
Figure 5. Quarterly bank revenues (in millions of EUR) and the cost/income ratio (rhs)



Strong capitalization of banks

As at 31 December 2014, the composite capital adequacy of credit institutions on solo basis was 35.7% and on consolidated basis 43.7% (respectively 20.0% and 24.4% in 2013). This great difference compared to the previous year was mostly caused by technical changes introduced to the calculation rules of capital adequacy indicators. Namely, in case of banks that directly applied the Internal Ratings-Based Approach, the minimum limit applicable during the transition period was not considered for the calculation of capital adequacy indicators as at 31 December 2014. In the future, this restriction should be taken into account in the calculations of individual minimum capital adequacy level of banks. Without considering the effect of these technical changes, the capital adequacy of the sector was 24.0% on solo basis and 28.9% on consolidated basis. Capital structure of the banking sector remained relatively simple and was still primarily based on Tier 1 capital. Tier 1 capital was thus on an adequate level both on solo and consolidated basis: Tier 1 capital was on solo basis 35.2% and on consolidated basis 43.1%. When considering the minimum limit applicable during the transition period, the respective indicators were 23.7% and 28.6% (respectively 19.7% and 24.2% in 2013) (See Figure 6).

Figure 6. Capital adequacy of banks and banking groups (%)



6.2. Insurance companies

In 2014, 8 non-life insurance companies, 4 life insurance companies and the Estonian Traffic Insurance Fund providing cross-border insurance were engaged in insurance business in Estonia on the basis of activity licence. Furthermore, 4 foreign insurance companies offered non-life insurance services and 1 foreign insurance company offered life insurance services through their local branches. A total of 460 providers of non-life insurance services and 102 providers of life insurance services have been entered into the register of providers of cross-border insurance services.

RSA insurance group decided to sell its Eastern European assets to the Polish insurance group PZU SA. That meant that the insurance portfolio of Codan Forsikring A/S Estonian (RSA) Branch was transferred to UAB DK PZU Lietuva Estonian Branch.

6.2.1. Non-life insurers

In 2014, the volume of gross premiums of non-life insurance companies totalled € 359.2 million, the annual increase being 2.9%. 55.1% of all insurance premiums were collected in Estonia, 18.5% were collected in Latvia and 26.4% in Lithuania. Benefits paid by non-life insurers amounted to € 199.4 million in 2014, the annual increase being 1.6% (See Figure 7).

Land vehicles insurance captured the biggest market share

The structure of non-life insurance portfolio has experienced no significant changes in recent years. Land vehicles insurance continues to capture the biggest market share. Property insurance and motor TPL insurance occupy the second and third place with equal volumes (See Figure 8). The share of accepted reinsurance in the insurance portfolio decreased in 2014 due to refunds caused by cancellations.

Branches increased their importance in non-life insurance market

Estonian non-life insurers collected insurance premiums within the amount of € 262.5 million, the annual growth being 6.8% in 2014. The market share of branches continued to grow in 2014 and the total share of branches reached to 24.4% of the market. Following the transfer of the insurance portfolio of Codan Forsikring A/S Estonian (RSA) Branch to UAB DK PZU Lietuva Estonian Branch, the market share of UAB DK PZU Lietuva Estonian Branch reached to 15% of the Estonian non-life insurance market and it achieved the third place by the volume of non-life insurance services (See Figure 9).

Figure 7. Insurance premiums by countries and paid benefits (in millions of EUR)

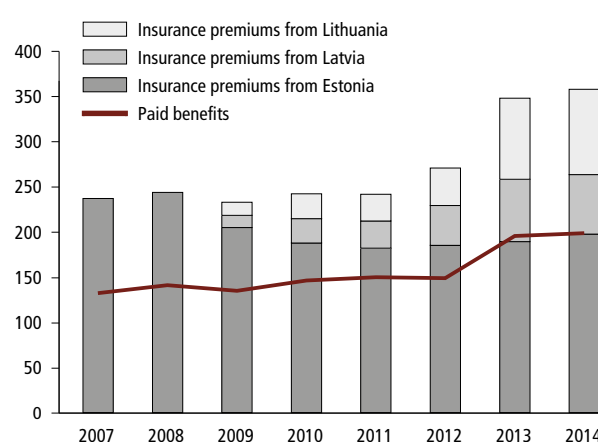


Figure 8. Structure of non-life insurance market in 2014 based on insurance premiums (in brackets 2013)

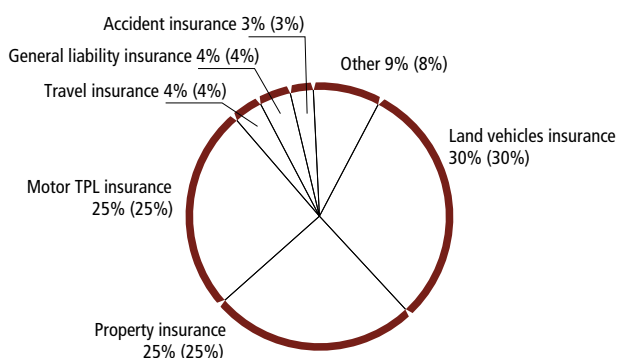
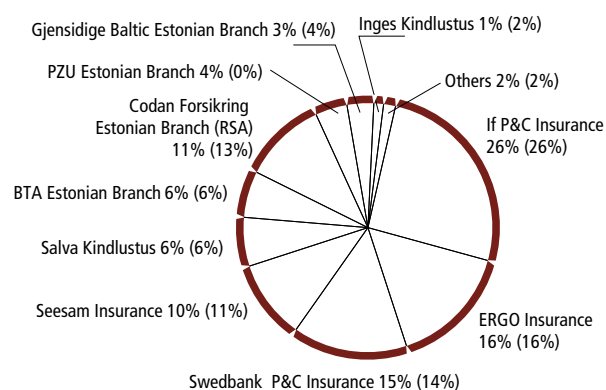


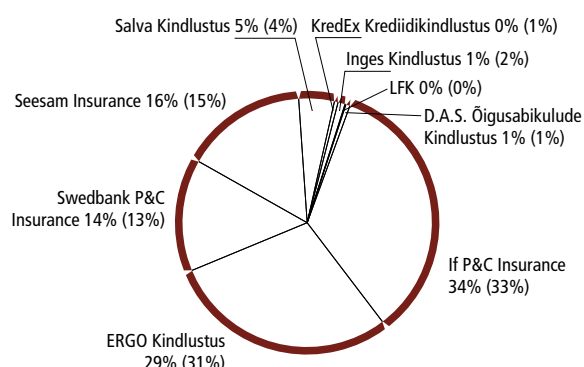
Figure 9. Market shares of non-life insurers by insurance premiums collected in Estonia, 2014 (in brackets 2013)



Baltic-wide companies captured the biggest market share

Asset volume of non-life insurers reached to € 593 million at the end of 2014, including investments within the amount of € 519.9 million. Technical provisions of non-life insurers (net of reinsurance) grew to € 273.3 million by the end of 2014 (See Figure 10).

Figure 10. Market shares of non-life insurers in 2014 by insurance premiums (in brackets 2013)

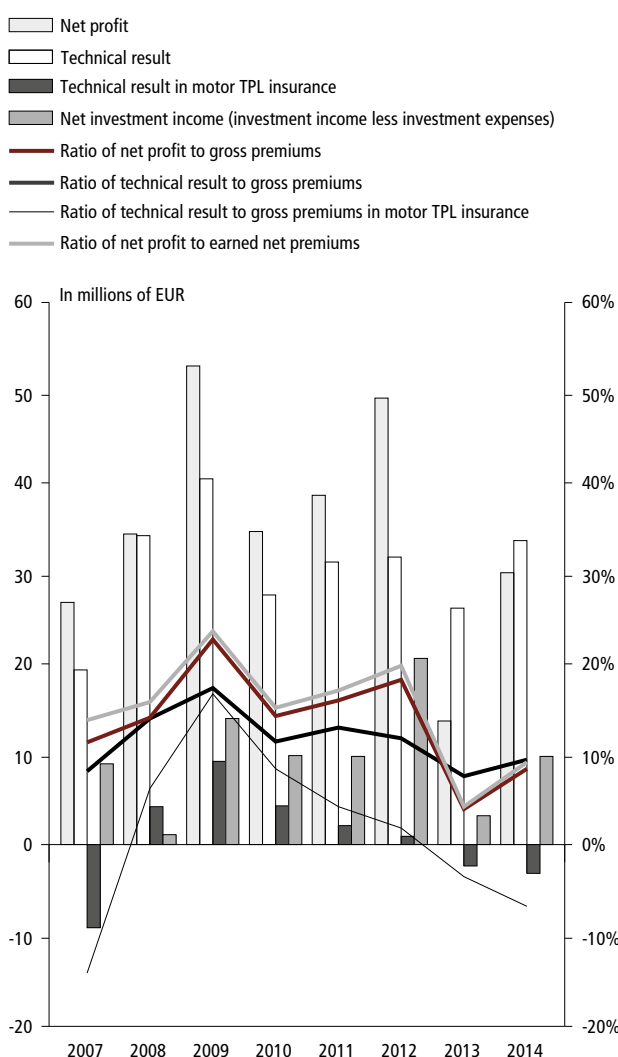


Growing net profits of non-life insurers

Non-life insurance profit⁷ amounted to € 30.2 million in 2014. Combined ratio⁸ dropped back below 90%. Technical profit earned by non-life insurance companies reached to € 33.7 million and investment result totalled € 9.7 million euro in 2014.

5 non-life insurers ended the year with net profit (See Figure 11).

Figure 11. Profit (technical profit) and profit margin (technical profit margin) of non-life insurers, 2007–2014



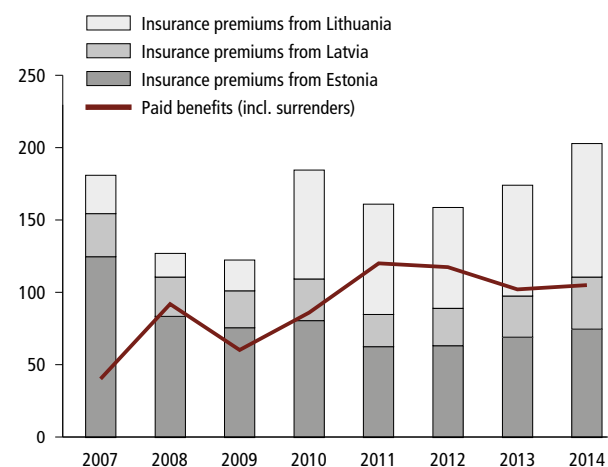
⁷ Unaudited data.

⁸ Combined ratio = loss ratio + expense ratio (gross figure includes reinsurance).

6.2.2. Life insurers

In 2014, life insurers collected € 201.8 million in insurance premiums and the volume of insurance premiums increased by 16.4%. 36.9% of premiums were collected in Estonia, 17.6% in Latvia and 45.4% in Lithuania. While the premium volume growth had been very similar in all three Baltic States in 2013 – 10% in a year as an average, the year 2014 witnessed some variances: the biggest growth in the premium volume occurred in Latvia where the annual growth was 25.4%, and the smallest growth was experienced in Estonia (only 8.1%). The premium volume growth in Lithuania was 20.6%. Benefits (including surrenders) were paid out within the amount of € 104.6 million (3% more than in 2013) (See Figure 12).

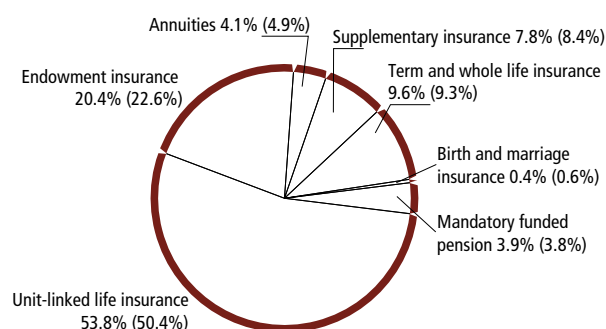
Figure 12. Insurance premium volume by countries and paid benefits (in millions of EUR)



Unit-linked life insurance captured the biggest market share

The structure of life insurance portfolio experienced no significant changes in 2014. Unit-linked life insurance continued to be the most popular insurance class, based on the volume of insurance premiums. Premium volume of unit-linked insurance accounted for over a half of all life insurance premiums (See Figure 13). Also, the growth in unit-linked life insurance was the biggest among life insurance classes in 2014: the collection of insurance premiums from unit-linked life insurance increased by 24% in comparison with the previous year.

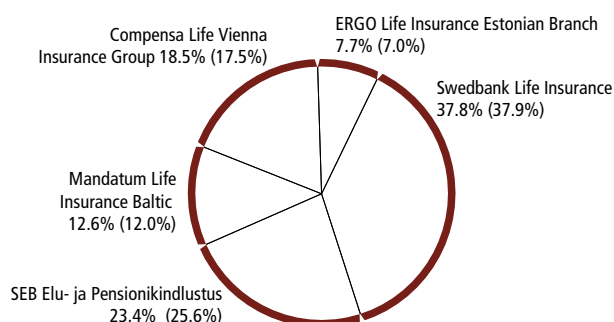
Figure 13. Structure of life insurance market in 2014 based on insurance premiums (in brackets 2013)



Estonian life insurance market grew by 9%

The total volume of Estonian life insurance market in terms of insurance premiums reached to € 80.8 million in 2014, the annual increase being 8.9% (See Figure 14).

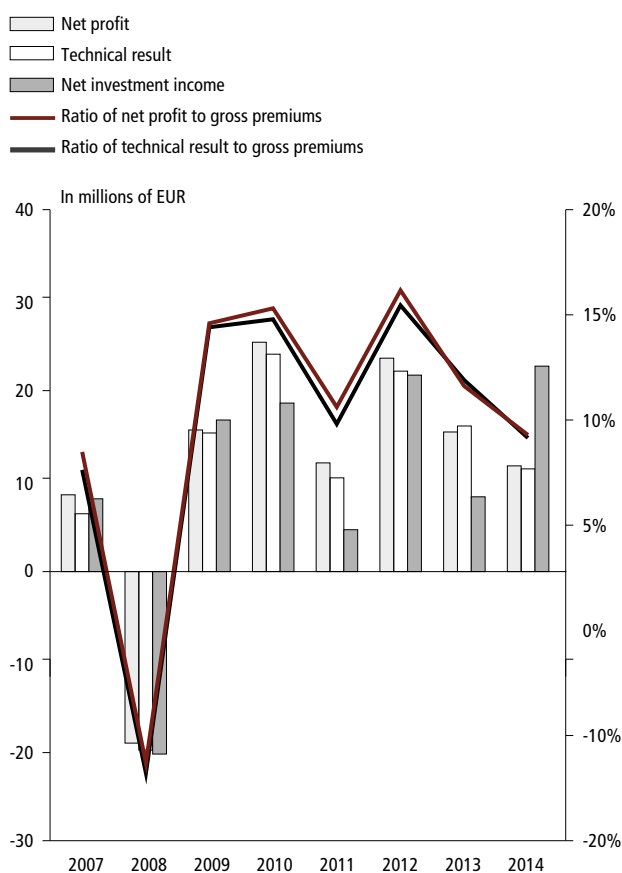
Figure 14. Market shares of life insurers in 2014 by insurance premiums collected in Estonia (in brackets 2013)



Life insurance profit dropped almost by a fourth

Total unaudited net profit of life insurers amounted to € 11.7 million and technical income totalled € 11.4 million (See Figure 15). Net profit received in 2014 was 24.5% less than in 2013. Decreasing profitability was caused by income tax paid on dividends and increased liabilities of life insurance companies due to abnormally low interest rate level.

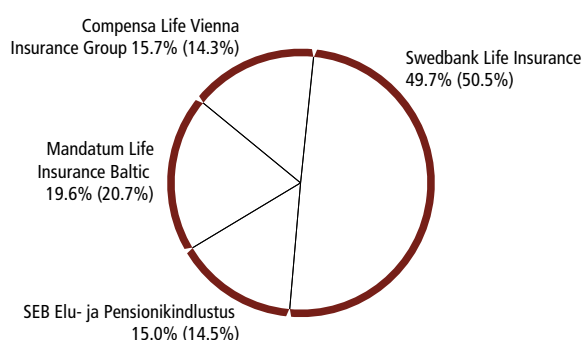
Figure 15. Profit (technical profit) and profit margin (technical profit margin) of life insurers, 2007–2014



Insurance liabilities increased

Financial liabilities of unit-linked life insurance contracts (i.e. the part of insurance liabilities where the risk is borne by policyholders) increased almost by 15% in 2014, from € 442.7 million to € 509.4 million. Technical provisions and guaranteed financial liabilities (i.e. the part of insurance liabilities where the risk is borne by insurer), increased almost by 10% during the year to the level of € 360.4 million by the end of 2014 (See Figure 16).

Figure 16. Market shares of life insurers in 2014 by insurance liabilities (in brackets 2013)



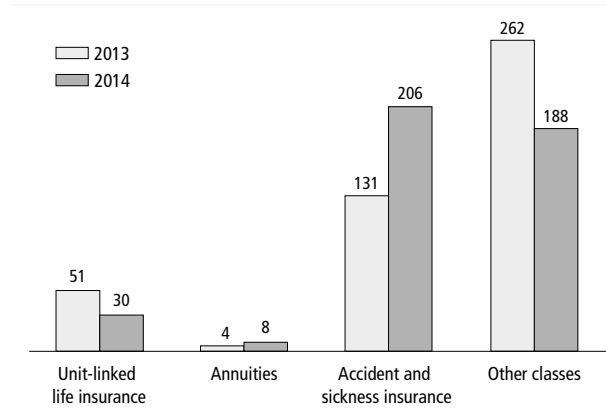
6.3. Insurance brokers

As at the end of 2014, 39 insurance brokers and 6 branches of foreign insurance brokers were engaged in Estonian market on the basis of activity license.

6.3.1. Life insurance

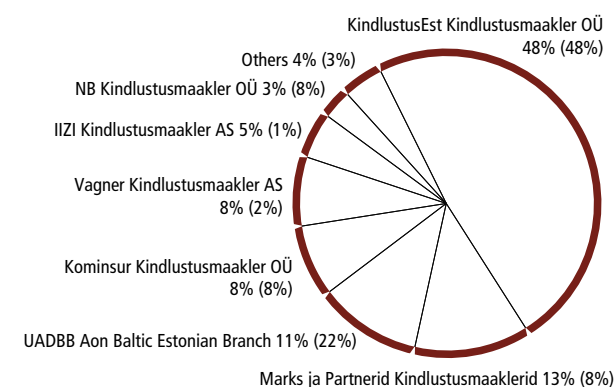
According to data available to the FSA, insurance brokers registered in Estonia mediated life insurance premiums within the amount of € 432,000 in 2014 (See Figure 17). Insurance brokers registered in Estonia mediated in total 602 life insurance contracts (473 contracts in 2013). The volume of mediated insurance premiums decreased by 4% in a year. Accident and sickness insurance contracts with premium volume of € 206,000 were the most mediated contracts in Estonian life insurance market in 2014.

Figure 17. Mediated insurance premiums by life insurance classes (in thousands of EUR)



In 2014, 10 insurance brokers mediated life insurance contracts (See Figure 18).

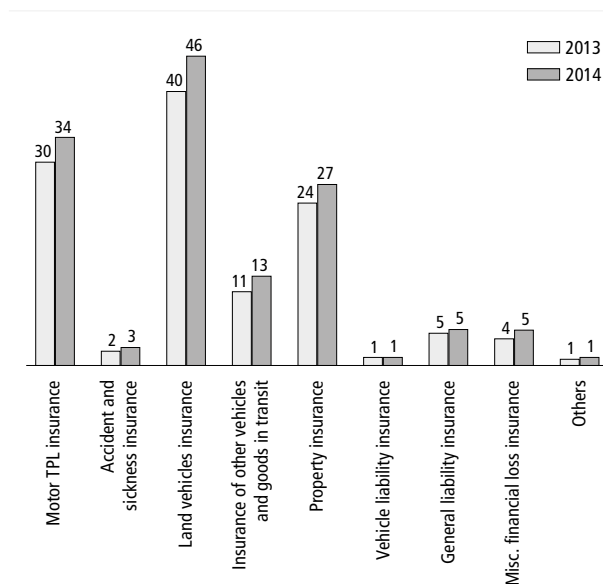
Figure 18. Market shares of insurance brokers in 2014 based on life insurance premiums (in brackets 2013)



6.3.2. Non-life insurance

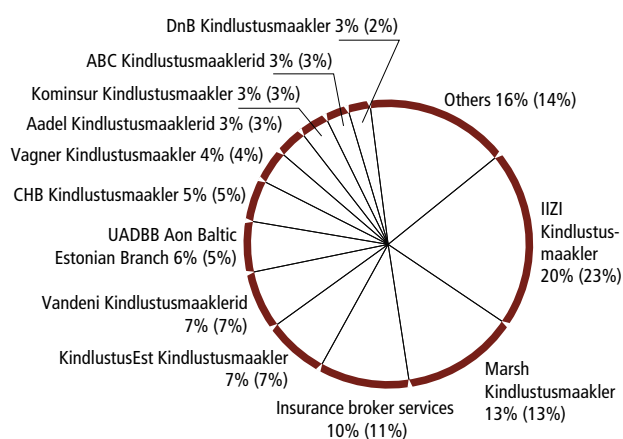
According to data available to the FSA, insurance brokers registered in Estonia mediated non-life insurance premiums within the amount of € 135 million⁹ in 2014. Annual increase in the volume of mediated insurance premiums was € 16 million. In 2014, the most mediated non-life insurance class based on the volume of mediated insurance premiums was the land vehicles insurance with € 46 million; it was followed by motor TPL insurance with € 34 million and property insurance with € 27 million (See Figure 19).

Figure 19. Mediated insurance premiums by non-life insurance classes (in millions of EUR)



37 insurance brokers mediated non-life insurance contracts in 2014 (See Figure 20).

Figure 20. Market shares of insurance brokers in 2014 based on non-life insurance premiums (in brackets 2013)



⁹ This report does not cover the contracts of foreign reinsurers that were mediated in Estonia. The respective premium volume was € 7.3 million in 2014.

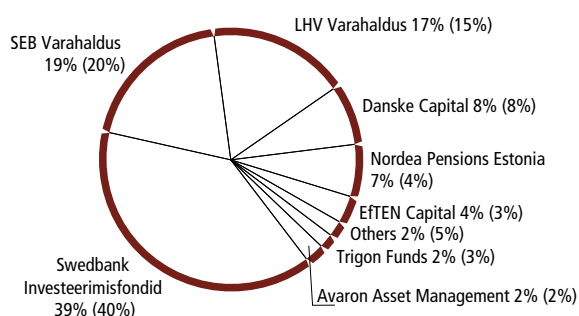


6.4. Fund management companies and funds

6.4.I. Fund management companies

18 authorized fund management companies were engaged in Estonian market at the end of 2014. Venture capital fund manager FB Asset Management AS entered the market. Pension fund manager ERGO Funds AS left the market and transferred its business to Nordea Pensions Estonia AS. Market concentration (calculated on the basis of the total fund volume of three major fund management companies) remained on the level of 75% in 2014 (See Figure 21).

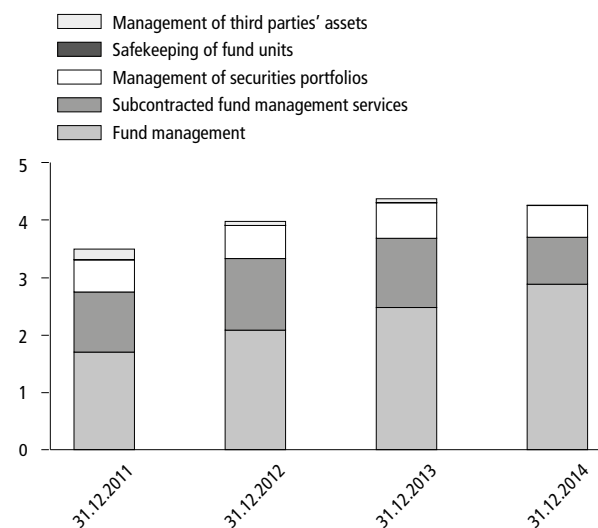
Figure 21. Market shares of fund management companies in 31.12.2014 based on investment funds' volumes (in brackets 31.12.2013)



Total volume of managed assets decreased by 3%

Total volume of funds increased by 16% in 2014, amounting to € 2.9 billion. Fund management services were provided under an outsourcing agreement also to funds which or the assets of which are not managed by fund management companies. The volume of assets managed under such subcontracted services agreements dropped by 32% to € 0.8 billion in 2014. Some fund management companies provided asset management services to third parties in respect of asset classes for which the management company has obtained the authority to manage a fund. The total volume of assets managed by fund management companies decreased from € 4.4 billion to € 4.3 billion in 2014 (data does not include investment consulting services) (See Figure 22).

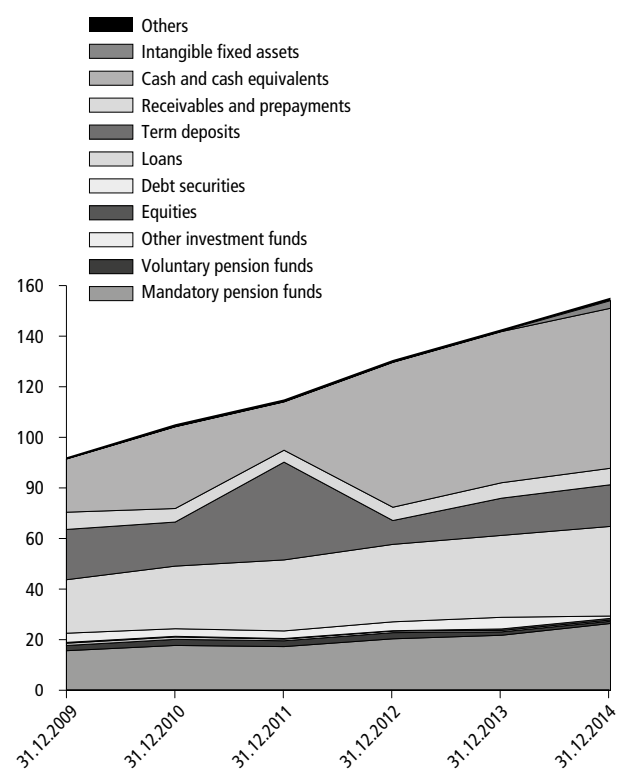
Figure 22. Managed assets by business lines (in billions of EUR)



Aggregated balance sheet volume of fund management companies grew by 9%

Total asset volume of fund management companies amounted to € 156 million at the end of 2014. The structure of aggregated balance sheet remained relatively stable during the year: as before, cash and cash equivalents and term deposits captured the biggest shares of assets. The 23% share of loans was also significant, but this asset class was dominated by intra-group loans. Investments of fund management companies into units of funds managed by them were more receptive to fluctuations on financial markets. Asset structure was very diverse among different fund management companies (See Figure 23).

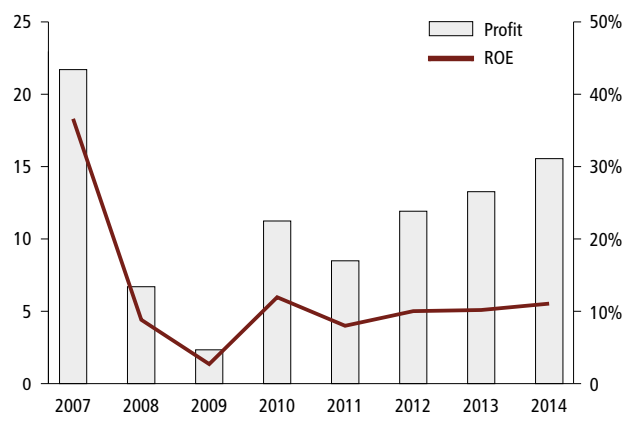
Figure 23. Aggregate balance sheet structure of fund management companies (in millions of EUR)



Commission income supported profitability in the sector

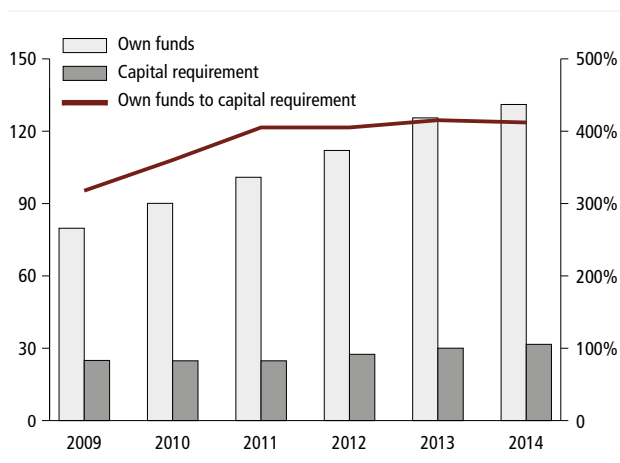
Based on unaudited data, the sector of fund management companies earned the profit of € 15.6 million in 2014, which was 17% more than in the previous year. In 2014, both gross commission income and commission costs as well as fixed overhead costs increased. Profit earned in the sector was primarily supported by net commission income that grew faster than fixed overhead costs. The ratio of fixed overhead costs to net commission income decreased from 52% to 50% in 2014. In addition, profits earned from fund managers' own financial investments increased. Return on Equity of the sector grew from 10% to 11% (See Figure 24).

Figure 24. Profit (in millions of EUR) and ROE (%) of the fund management companies sector



As at the end of 2014, all fund management companies offering pension fund management services complied with requirements established for the ownership of pension fund units. The total volume of the own funds of fund management companies was more than four times higher than the capital required – the coverage of minimum own funds requirement was 414% at the end of 2014 (See Figure 25).

Figure 25. Capitalisation of fund management companies sector
(min 100%)



6.4.2. Investment and pension funds

The year 2014 witnessed 2 mergers of mandatory pension funds and equity funds. 2 new hedge funds and one real estate fund entered the market and one real estate fund was liquidated. There were 65 investment and pension funds registered in Estonia at the end of 2014 (See Table).

Investment and pension funds registered in Estonia

Fund type	31.12.2013	31.12.2014
Equity funds	22	20
Hedge funds	2	4
Debt funds	3	3
Real estate funds	8	8
Mandatory pension funds	23	20
Money market funds	0	0
Voluntary pension funds	13	10
Total	71	65

Number of mandatory pension fund unit holders the biggest

The number of pension fund unit holders started to increase after several years of decline, growing from 770,502 to 781,009 (See Table). The number of mandatory pension fund unit holders increased by 12,849 in 2014. However, for other types of funds, numbers of unit holders still demonstrated a declining trend. The biggest drop was experienced by equity funds for several years in a row – the number of unit holders decreased by 1,641 in 2014. Also, the number of voluntary pension fund unit holders decreased from 44,716 to 44,291. A significant drop occurred in the number of real estate fund unit holders – from 292 to 104; this was mainly caused by the liquidation of one of the funds.

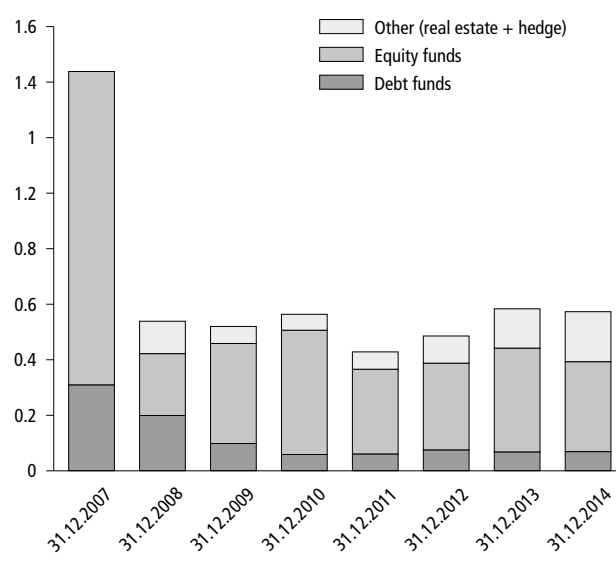
Number of unit holders by different fund types

Fund type	31.12.2013	31.12.2014
Equity funds	15,813	14,172
Hedge funds	282	292
Debt funds	587	492
Real estate funds	292	104
Mandatory pension funds	708,812	721,658
Voluntary pension funds	44,716	44,291
Total	770,502	781,009

Net asset value of pension funds increased

Following the financial crisis of 2007, net asset value of investment funds registered in Estonia has increased only in the pension funds sector. Net asset value of other investment funds has stayed on the level of € 0.6 billion during the last six years (See Figure 26).

Figure 26. Net asset value of investment funds (except pension funds) (in billions of EUR)



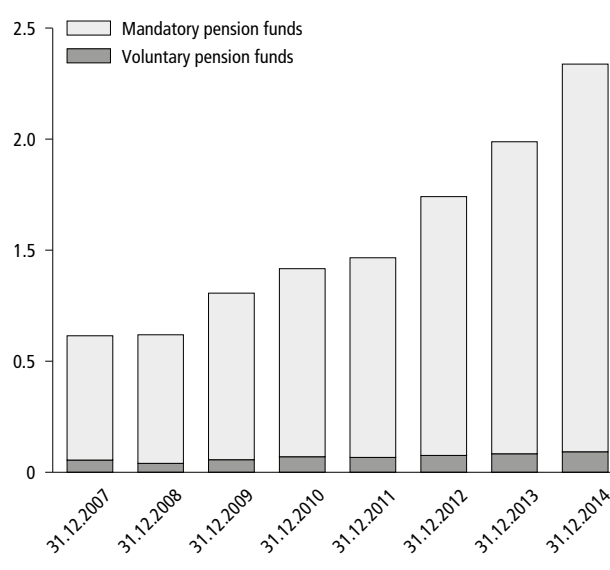
Net asset value of other investment funds experienced an annual decline of 2% (€ 10 million). Assets of investment funds amounted to € 574 million in 2014.

Decline in the asset volume was mainly caused by decreasing net asset value of equity funds that dropped from € 374 million at the beginning of 2014 to € 324 million at the end of 2014 (annual decline of 13%). This drop in the asset volume of equity funds was somewhat balanced out by the increase of € 41 million in the asset volume of hedge funds.

Net asset value of mandatory pension funds increased by 24% in 2014 – from € 1.8 billion to € 2.2 billion. The asset volume of mandatory pension funds increased by € 36 million per month as an average, i.e. the growth was bigger than in 2013 when the growth rate of assets of II pillar pension funds was € 26 million per month as an average.

Asset volume of voluntary pension funds grew by 12% or € 13 million in 2014 to the level of € 117 million at the end of the year (See Figure 27).

Figure 27. Net asset value of pension funds (in billions of EUR)

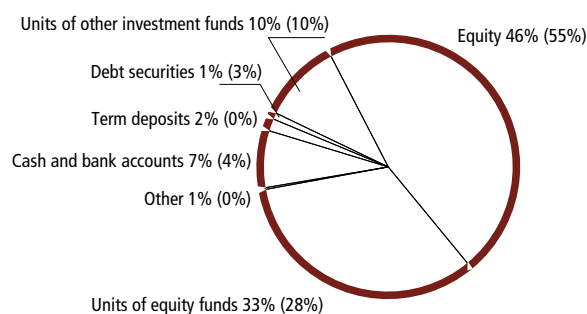


Considerable share of investments still made through other funds

Investment and pension funds registered in Estonia tend to invest through other investments funds and avoid making direct investments into securities. As at 31 December 2014, direct investments accounted for 33% of the composite portfolio of investment and pension funds, whereas investments through other funds accounted for 51% of the composite portfolio. If we compare equity risk and interest rate risk, we can notice that equity risk decreased in 2014. Equity and interest rate risk accounted for 42% and 41% (respectively) of the volume of funds' composite portfolio at the year-end.

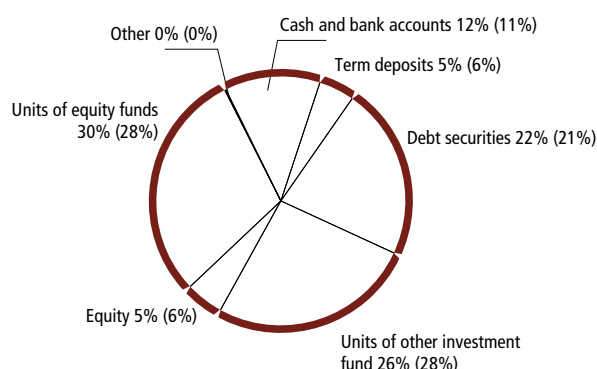
Equity funds are considered the biggest type of investment funds by asset volume. Most of the investments made by equity funds are direct investments. However, the share of equity investments dropped from 55% to 46% in 2014 and the share of debt investments decreased from 3% to 1%. Investments made through other funds continued to demonstrate an increasing trend in 2014 and accounted for 43% of investments at the year-end, whereas 33% of investments were made through equity funds and 10% were made through other investment funds¹⁰ (See Figure 28)

Figure 28. Asset structure of equity funds, 31.12.2014
(in brackets 31.12.2013)



The majority of investments of mandatory pension funds are made through other funds and this trend continued in 2014. Direct investments into securities accounted for 27% and investments made through other funds accounted for 56% of the composite portfolio at the year-end (See Figure 29).

Figure 29. Asset structure of mandatory pension funds, 31.12.2014
(in brackets 31.12.2013)



The composite portfolio of voluntary pension funds was also dominated by investments made through other funds, accounting for 81% of the assets at the end of 2014.

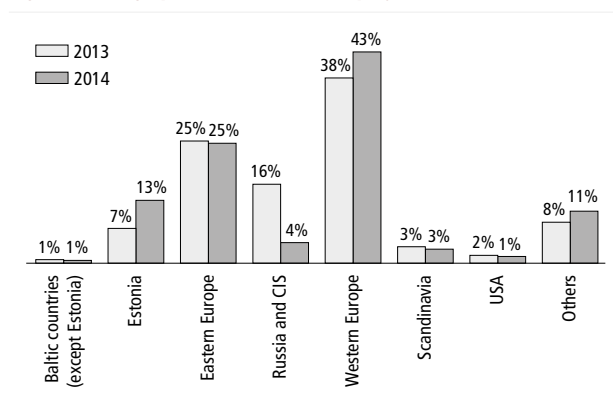
¹⁰ Income and real estate funds.

Dominating investments to European markets

Although the investments of investment and pension funds registered in Estonia are characterised by their global nature, most of them still target Europe or are made through funds that are registered in European financial centres.

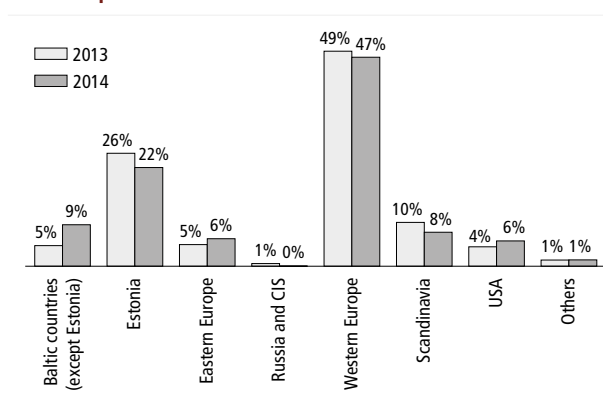
As at 31 December 2014, 43% of assets of equity funds were invested into Western European issuers and 25% were invested into Central and Eastern European markets. The volume of investments made into Russian and CIS markets experienced a significant drop, decreasing from 16% to 4%. Investments into instruments registered in Estonia increased from 7% to 13%. Direct investments into securities registered in Estonia accounted for 2% of the composite investment portfolio of equity funds at the end of 2014 (See Figure 30).

Figure 30. Geographical distribution of equity funds' investments



As to the investments made by mandatory pension funds, the biggest increase was demonstrated by the aggregate share of Latvian and Lithuanian issuers – from 5% to 7% in 2014. The share of US issuers reached from 4% to the level of 6%. Investments made into Estonian markets somewhat decreased in 2014 – from 26% to 22% of the total asset volume. Term deposits and bank accounts formed the biggest share (17%) of mandatory pension funds' assets. Direct investments into securities registered in Estonia accounted for 3% of the portfolio and investments into funds registered in Estonia (mostly into funds that focused on Eastern European markets) accounted for another 3% of the total asset volume of mandatory pension funds. Mandatory pension funds made the biggest investments into Western European issuers; however, their share decreased from 49% to 47% in 2014 (See Figure 31).

Figure 31. Geographical distribution of investments of mandatory pension funds



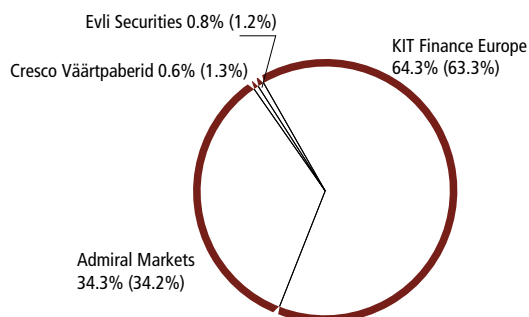
6.5. Investment firms

High concentration risk of investment firms' assets

In 2014, 4 investment firms operated in Estonia under the activity license issued by the FSA. Evli Securities AS initiated a liquidation proceeding in December 2014.

Asset volume of investment firms amounted to € 66 million (See Figure 32): deposits held in banks and financial institutions accounted for 63% and securities-backed-loans to clients accounted for 33% of these assets. High concentration risk of investment firms was caused by assets held in Russian financial institutions. Investments into securities accounted only for 0.4% of investment firms' assets.

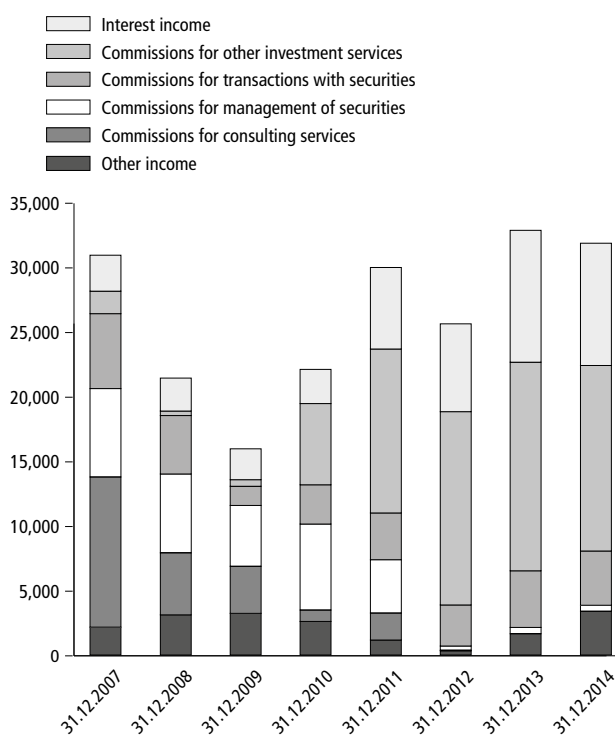
Figure 32. Market shares of investment firms by asset volume, 31.12.2014 (in brackets 31.12.2013)



Decreasing profitability

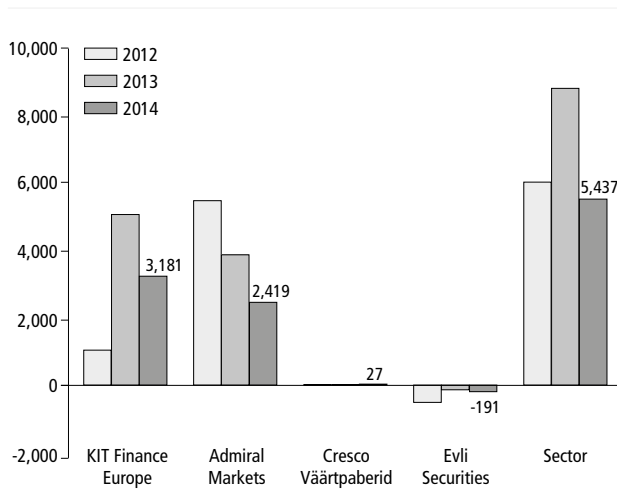
Investment firms earned income within the amount of € 32 million in 2014 or 3% less than in 2013. The majority of income (60%) was earned from the mediation of clients' transactions with securities. Interest income amounted to 29% (See Figure 33).

Figure 33. Commissions of investment firms by types (in thousands of EUR)



Profits of investment firms totalled € 5.4 million in 2014, the annual decrease was 37% (See Figure 34). This abrupt drop in the profitability of investment firms was caused by decreasing interest income, increasing commission costs and income tax paid on dividends.

Figure 34. Annual net profit (loss) of investments firms
(in thousands of EUR)



6.6. Payment institutions

12 payment institutions authorised by the FSA were conducting business in Estonia at the end of 2014. Five of them had received a special license that allowed the application of lower regulative requirements and limited the volume of mediated payments.

In 2014, the FSA issued a license for the provision of money remittance services to the subsidiary of AS Tavid, the TavexWise AS. A special license was issued to Kambja Hoiu-Laenuühistu.

Two major payment institutions captured the market share of 95.3% (See Figure 35).

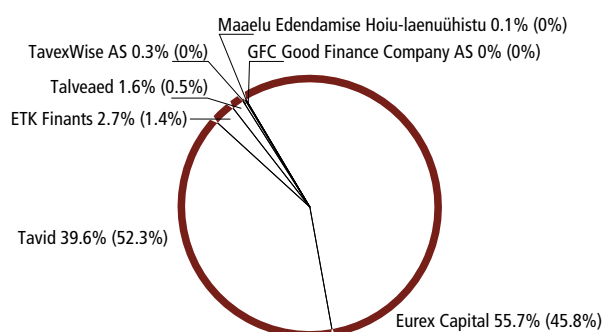
Decrease in payments volume for the third year in a row

In 2014, fully licensed payment institutions mediated payments within the amount of € 916 million. The volume of payments dropped by 8.5% in comparison with 2013.

Payment institutions earned mostly profits

While 2013 had been an unprofitable year for the sector as a whole, in 2014 most of the payment institutions earned profits. Profits of payment institutions totalled € 3.9 million in 2014. Return on Equity (ROE) of the sector was 9.9%.

Figure 35. Market structure of payment institutions by payments volume in 2014 (in brackets 2013)



6.7. Securities market operator

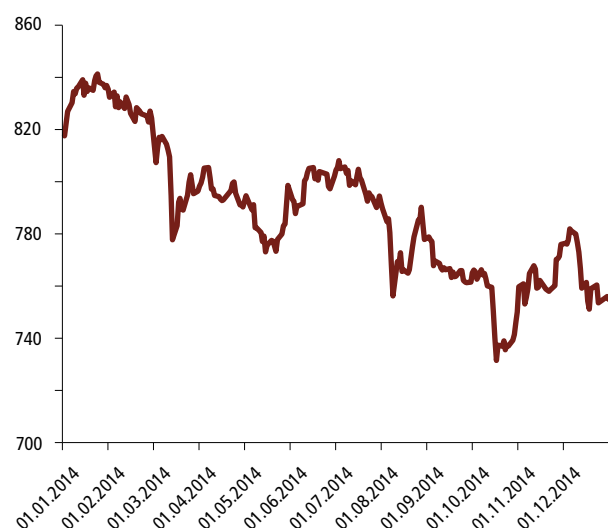
6.7.1. NASDAQ OMX Tallinn Stock Exchange

Decreasing trading activity compared to the previous year

In 2014, the index of NASDAQ OMX Tallinn Stock Exchange decreased by 7.66% to the level of 755.05 points.

The price index of leading shares traded on European stock exchanges – Dow Jones EURO STOXX 50 – increased by 1.20% in 2014 (See Figure 36).

Figure 36. OMXT index in 2014



Trading activity on NASDAQ OMX Tallinn Stock Exchange slowed down in comparison with the previous year and total turnover amounted only to € 127.3 million (€ 60.3 million less than in 2013).

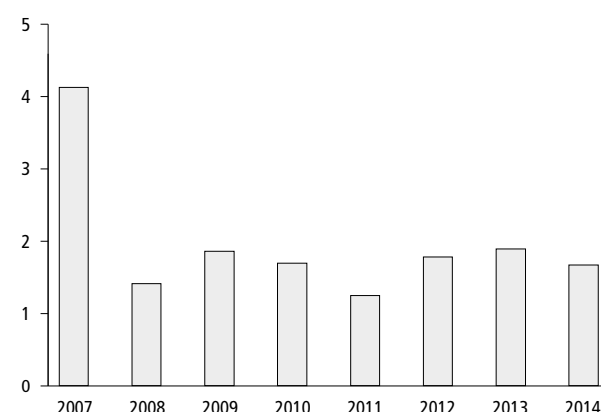
The biggest gainers in the main list were the shares of AS Tallinna Vesi (+10.08%) and AS Harju Elekter (+3.33%). The price of AS Silvano Fashion Group (-55.81%) and Arco Vara AS (-40.86%) shares decreased the most.

The shares of AS Järvevana were delisted in the last quarter of 2014 as a result of successful takeover bid.

Market capitalisation decreased

Market capitalisation of NASDAQ OMX Tallinn Stock Exchange was € 1.66 billion at the end of 2014 (€ 1.8 billion at the end of 2013). Market capitalisation decreased by € 140 million in comparison with 2013 (See Figure 37). This drop in capitalisation level was primarily driven by the annual decrease in share prices and the delisting of the shares of AS Järvevana.

Figure 37. Market capitalisation of Tallinn Stock Exchange (in billions of EUR)



Fewer transactions on the Stock Exchange

At the end of 2014, there were the shares of 13 companies included in the main list of NASDAQ OMX Tallinn Stock Exchange and 2 companies in the additional list.

There were 43,227 transactions made with shares of Tallinn Stock Exchange in 2014, the annual decline being 14.4% (50,473 transactions in 2013). The turnover of NASDAQ OMX Tallinn Stock Exchange was € 127.3 million in 2014, the annual decrease being 32.1% (€ 187.6 million in 2013).

Trading was the most active with the shares of Olympic Entertainment Group, followed by the shares of AS Tallink Grupp and AS Silvano Fashion Group. Tallinn Stock Exchange had 24 members at the end of 2014.

The most active members on NASDAQ OMX Tallinn Stock Exchange were Swedbank AS (37.22%) and AS SEB Pank (29.37%) by turnover in 2014. Swedbank AS was the most active also by the number of transactions, making 33.08% of all transactions (See Figures 38 and 39).

Figure 38. Structure of Tallinn Stock Exchange by participants in 2014

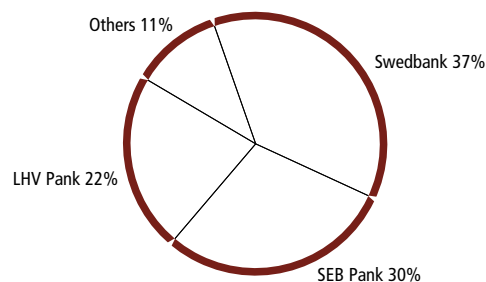
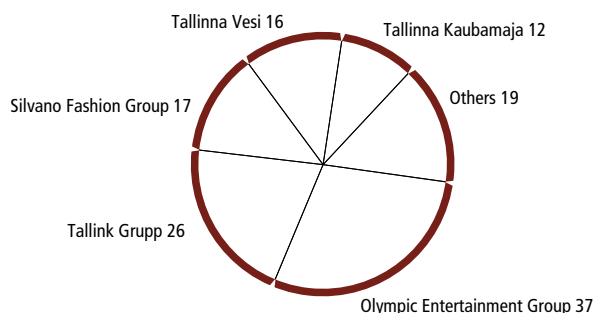


Figure 39. Structure of Tallinn Stock Exchange by traded shares in 2014 (in millions of EUR)



6.7.2. Estonian Central Register of Securities

The Estonian Central Register of Securities, founded in 1994, is the central electronic register of Estonian securities and the administrator of the register for pension funds in Estonia, and it keeps all securities accounts and pension accounts opened in Estonia and the share registers of all public limited companies operating in Estonia. It also administers the acceptance of applications for the mandatory funded pension or II pillar of the pension system, and the issuance of fund units. The owner of the Estonian Central Register of Securities is NASDAQ OMX Tallinn AS that belongs into the group of NASDAQ OMX.

There were 106,466 valid securities accounts registered with the Estonian Central Register of Securities at the end of 2014. The number of securities accounts decreased by 911 accounts in a year. 93,235 of securities accounts belonged to individuals.

As to the country of origin of investors, the share of Estonian investors increased from 58.4% to 59.9% in 2014. Investors from Luxembourg came second with 11.1%, followed by investors from the Cayman Islands with 6.7% and from the Netherlands with 5.6%.

Annex

Organisational structure of
the Financial Supervision Authority

