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European Bank
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Corporate Governance in Transition Economies

Latvia Country Report

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The Report is based on information available at the end of April 2015.

If you believe that the information has changed or is incorrect, please contact Gian Piero Cigna at cignag@ebrd.com

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This Report – along with all other country reports prepared within this initiative – is available at: http://www.ebrd.com/what-we-do/sectors/legal-reform/corporate-governance/sector-assessment.html

Foreword

As part of its Legal Transition Programme, the European Bank for Reconstruction and Development ("EBRD") has been assessing the state of legal transition in its countries of operations. These assessments provide an analysis of the progress of reform and identify gaps and future reform needs, as well as strengths and opportunities.

In 2012, the Legal Transition team within the EBRD Office of the General Counsel (LTT) developed with the Assistance of Nestor Advisors a methodology for assessing corporate governance frameworks and the governance practices in the EBRD countries of operations. This assessment was implemented in 2014-2015 (the "Assessment").

The Assessment aims at measuring the state of play (status, gaps between local laws/regulations and international standards, effectiveness of implementation) in the area of corporate governance

The Assessment is meant to provide for (i) a comparative analysis of both the quality and effectiveness of national corporate governance legislation (including voluntary codes); (ii) a basis to assess key corporate governance practices of companies against the national legislation; (iii) an understanding whether the legal framework is coupled with proper enforcement mechanisms (e.g., sanctions) and/or with authorities able to ensure proper implementation; (iv) a support to highlight which are the major weaknesses that should be tackled by companies and legislators for improving the national corporate governance framework; and (v) a tool which will enable the EBRD to establish "reference points" enabling comparison across countries.

This country report is part of a series of 34 country reports. A general report synthesising all countries will close the Assessment.

Methodology

This Assessment is based on a methodology designed to measure the quality of legislation in relation to best practices requirements and the effectiveness of its implementation as evidenced by companies' disclosure, also taking into consideration the capacity of the institutional framework (e.g., courts, regulators) to sustain quality governance. The analytical grid developed for assessing the governance framework is based on international recognised best-practice benchmarks (e.g., OECD Corporate Governance Principles, Development Financial Institutions, EBRD, IFC and World Bank ROSC governance methodologies). The methodology is applied identically across all the countries reviewed. The process for gathering, analysing and reporting information is applied identically for each of the countries assessed, which allows comparing countries to each other across a long a set of benchmarking points.

For the purpose of the Assessment, the corporate governance framework and the practices were divided in five key areas: (i) Structure and Functioning of the Board; (ii) Transparency and Disclosure of company information; (iii) Internal Control; (iv) Rights of Shareholders; and (v) Stakeholders and Institutions. Each of these key areas is further divided in sections (for instance, the area "Structure and Functioning of the Board" is divided in five sections: Board composition; Gender diversity at the board; Independent directors; Board effectiveness; and Responsibilities of the board). Each section is further divided in subsections (for instance, the section "Independent Directors" is divided in three subsections: "Requirement to have independent directors"; "Definition of Independence"; and "Disclosed practices").

The assessment started by sending a questionnaire to law firms, audit firms, national regulator(s), ten largest (listed) companies, and stock exchange(s) in each country. Questions were different according to the respondents, which were asked to provide information on the legislation and on how they believe the legislation is implemented.

Responses were assigned to the corresponding subsection(s) and validated by the EBRD corporate governance specialists by looking at the applicable framework and at the disclosure offered by the ten largest (listed) companies in each country. In this respect, the working hypothesis was that the ten largest listed companies are those offering the best disclosure in each country. As such, we presumed that when certain practices were not disclosed by them, they were unlikely to be disclosed by smaller or unlisted companies. The ten largest companies were identified according to their market capitalisation. When a country did not have a stock exchange, there were less than ten listed issuers or there were no data on capitalisation of issuers, the ten largest companies were identified according to their revenues and size of the labour force. In case the largest companies were mostly of one sector (e.g., financial institutions), then the sample of ten companies was corrected to reflect other sectors of the economy.

The validation of responses was undertaken by the corporate governance specialists within the Legal Transition Team through desktop research. This research was conducted both on legislation and on the practices disclosed by the largest (listed) companies (e.g., companies' websites, annual reports, stock exchanges database etc.). In addition, the relevant reports by international financial institutions (e.g., IMF, World Bank, IFC, Transparency International, etc.) were analysed and taken into consideration. Answers received by respondents that were not grounded by specific references to legislation or consistent with the disclosed practices were not taken into consideration.

Following the validation process, each subsection was compiled by adding specific references to legislation and practices. Conclusions were then formulated for each subsection, each rated as per their adherence to international governance standards. The score ranges from 1 (very weak) to 5 (strong). The rating for each section was then calculated by averaging the ratings of the subsections.

Because understanding corporate governance requires a "holistic perspective", where each component needs to have a place in the overall picture – pretty much like a puzzle - in case one of the subsection was rated "weak" or "very weak", the resulting average was decreased by 0.2; in case

more than one subsection was rated "weak" or "very weak", the resulting average was decreased by 0.5. This is because if just one component is not fitting well with the others, then all others are weakened. Similarly, the overall strength diminishes if there are more weak components.

Conversely, in order for the framework to be strong, all components need to be well fitting with each other. Hence, in case all subsections were scored "moderately strong" or "strong", then the resulting average was increased by 0.5. However, this "positive" adjustment was used with some care as the assessment looked at the top ten largest companies in the country, hence findings tended to be often overly optimistic.

Key areas were then rated according to the same criteria.

The ratings are presented through the colours detailed in the box below and they demonstrate the adequacy or need of reform in respect to each governance area and section.

Rating:

"Strong to very strong" (DARK GREEN) - The corporate governance framework / related practices of companies are fit-for-purpose and consistent with best practice.

"Moderately strong" (LIGHT GREEN) - Most of the corporate governance framework / related practices of companies are fit-for-purpose but further reform is needed on some aspects.

"Fair" (YELLOW) - The corporate governance framework / related practices of companies present some elements of good practice, but there are a few critical issues suggesting that overall the system should be assessed with a view of reform.

"Weak" (ORANGE) - The corporate governance framework / related practices of companies may present few elements of good practice, but overall the system is in need of reform.

"Very weak" (RED) - The corporate governance framework / related practices of companies present significant risks and the system is in need of significant reform.

We believe corporate governance cannot be captured and measured simply by numerical values. Hence, alongside the "quantitative" assessment obtained according to the methodology described above, a "qualitative" assessment was also undertaken, by classifying our findings for each section as "strengths" and "weaknesses". Because understanding corporate governance requires a "holistic perspective", when the "quantitative" assessment was finalised, the assessment team compared it with the "qualitative" assessment, and when any inconsistency (i.e. material weaknesses or strengths) was noticed, the average scores of the sections were adjusted by up to ±0.5.

A preliminary version of the Assessment was made public for consultation. The comments and corrections received during the process were analysed by the corporate governance specialists. When confirmed, the corrections were reflected in the final ratings and in this Assessment.

Overview

Legislative Framework

The primary sources of corporate governance legislation in Latvia are the Civil Code; the Commercial Law; the Law on Sworn Auditors; the Law on Financial Markets Instruments; and the Law on Annual Accounts and Reports. In 2005 the Riga Stock Exchange adopted the "*Principles of Corporate Governance and Recommendations on their Implementation*". The Principles have been reviewed and amended in 2008 and in 2010. Listed companies are required by law to disclose in their annual reports the extent to which they comply with the Principles and in case on non-compliance explain the reasons for such non-compliance (so called "*comply or explain*" approach). This approach appears to be well implemented – all ten largest listed companies have submitted a "*comply or explain*" statement – and most of the explanations provided by companies are meaningful, but there is still room for improvement. In particular, it would be beneficial to start monitoring disclosure by companies on how companies "comply or explain" and issue an annual monitoring/guidance report on the subject.

Structure and Functioning of the Board

Joint stock companies are organised under a two-tier system, where the board appoints the management. In companies, the law does not explicitly empower the board to approve the company's budget, strategy and risk profile. The Principles recommends that these functions should be undertaken by the board. However, the law for banks is more precise in this respect. Boards are generally small and legal entities cannot be board members. Companies are not required by law to have independent board members but the "Principles of Corporate Governance and Recommendations on their Implementation" (i.e., the Latvian Corporate Governance Code) recommend companies to have a majority of independent directors. Half of the ten largest listed companies disclose having independent board members, but only in three cases independent directors represent the majority of the board. The Principles also include a definition of independence.

Public interest entities are required to have an audit committee, however it is not necessarily a board committee, as "outsiders" (i.e., non-board members) can sit on the committee. Disclosure on the audit committee composition and functioning is minimal and not sufficient to establish if they are playing a strategic role at the board. Banks are also required to have a risk committee and a nomination committee. Gender diversity on the board is among the highest in the EBRD region. There is no established practice of board evaluation, and companies do not disclose having a corporate secretary. Fiduciary duties, liability of board members and conflicts of interest are regulated by law, and it seems there is case law and judicial practice on these issues.

Transparency and Disclosure

Disclosure requirements are detailed in the law and appear to be generally well implemented. However, information on beneficial ownership, board's activities and audit committee's activities and meetings is not systematically disclosed. The law requires companies to prepare and disclose their financial information in line with IFRS, and all ten largest listed companies appear to comply with this requirement. The law details the disclosure requirement to the market and to shareholders. The law appears to be well implemented, also thanks to the Official Storage System, a publicly available internet portal, which includes information on the general shareholders' meeting.

Listed companies are also required by law to disclose their compliance with the Principles (under the "comply or explain" approach") and it appears that all ten largest listed companies included a corporate governance statement in their annual reports, with explanations in case of non-compliance. Explanations are often meaningful, but sometimes there are some clear misunderstandings of the Principles.

Companies are required to disclose detailed information on the external auditor, and auditors are required to make a yearly declaration of independence to the audit committee. Companies appear to comply with the requirements of the law, however some doubts arise with reference to rotation of auditors and provision of non-auditing services. Companies do not appear to have codes of ethics in place.

Internal Control

Banks are required to create internal audit and compliance functions. Other companies might appoint an internal audit and/or a company controller, but these functions are created upon shareholders' request and

are different from what is generally understood as internal audit. Public interest companies must establish an audit committee, but it is not necessarily a board committee, as it can include "outsiders" (i.e., non-board members), a common practice in Latvia. We do not think this is ideal.

External auditors are required to be independent, but they are allowed to provide non-auditing services. Rotation of external auditors is required, but this requirement does not seem to be well implemented. None of the ten largest listed companies disclose having codes of ethics in place. Whistleblowing legislation is not comprehensive. Related party transactions and conflicts of interest are regulated by law. The competence to approve related party transactions is assigned to the board and in some cases to the general shareholders' meeting. There is no requirement for the audit committee to review related party transactions.

Rights of Shareholders

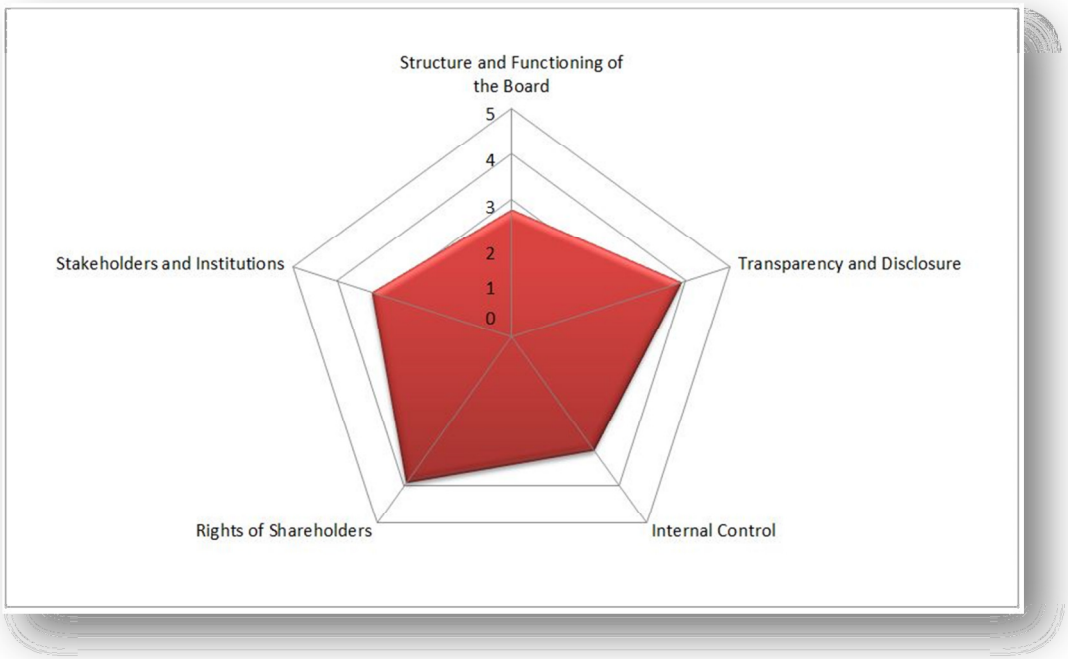
Basic shareholders rights are granted by law and generally well implemented. Minority shareholders can call a general shareholders meeting (GSM), nominate board members, request cumulative voting and start a derivative suit. Major corporate changes require qualified majority. However, pre-emptive rights can be waived by simple majority. Insider trading and self dealing are regulated by law, which appears to be well enforced.

Regulation on minority shareholders protection and shareholders' access to information seem to be comprehensive and generally in line with best practices. Explanations provided in the "comply or explain" reports are generally meaningful. Share register for listed companies is maintained by an independent registry institution. Shareholders agreements must be disclosed; however, they are rarely used and not much regulated. They are generally considered to be enforceable between the parties, however there is no consolidated case law on the matter.

Stakeholders and Institutions

The stock exchange appears to have limited capitalisation and liquidity, but it is active in promoting good quality disclosure by listed companies. International law firms and audit firms have material presence in the country, but presence of rating agencies is limited. The Corporate Governance Principles appear to be comprehensive, regularly reviewed and relatively well implemented. However, their implementation does not seem to be actively monitored. It appears that the institutional framework supporting good corporate governance is generally sound. This is also confirmed by international organisations indicators. The only negative note appearing from the assessment – common to a number of countries – is the limited attention paid by listed companies to queries of potential investors and stakeholders, which might be a sign of the need to develop better investor relation departments of issuers.

Corporate Governance Legislation and Practices in Latvia



Source: EBRD, Corporate Governance Assessment 2016

Note: The extremity of each axis represents an ideal score, i.e., corresponding to the standards set forth in best practices and international standards (e.g., OECD Corporate Governance Principles). The fuller the 'web', the closer the corporate governance legislation and practices of the country approximates best practices.

Key: Very weak: 1 / Weak: 2 / Fair: 3 / Moderately Strong: 4 / Strong to very strong: 5

Key Areas and Rating	Strengths and Weaknesses
1. Structure and Functioning of the Board *Fair*	*Joint stock companies are organised under a two-tier system, where the board appoints the management. In companies, the law does not explicitly empower the board to approve the company's budget, strategy and risk profile. The Principles recommends that these functions should be undertaken by the board. However, the law for banks is more precise in this respect.* *Boards are generally small and legal entities cannot be board members. Companies are not required by law to have independent board members but the "Principles of Corporate Governance and Recommendations on their Implementation" (i.e., the Latvian Corporate Governance Code) recommend companies to have a majority of independent directors. Half of the ten largest listed companies disclose having independent board members, but only in three cases independent directors represent the majority of the board. The Principles also include a definition of independence.* *Public interest entities are required to have an audit committee, however it is not necessarily a board committee, as "outsiders" (i.e., non-board members) can sit on the committee. Disclosure on the audit committee composition and functioning is minimal and not sufficient to establish if they are playing a strategic role at the board.* *Banks are also required to have a risk committee and a nomination committee.* *Gender diversity on the board is among the highest in the EBRD region.* *There is no established practice of board evaluation, and companies do not disclose having a corporate secretary.* *Fiduciary duties, liability of board members and conflicts of interest are regulated by law, and it seems there is case law and judicial practice on these issues.*
1.1. Board Composition *Moderately strong*	***Strengths:*** • *Joint stock companies are organised under a two-tier system, where the board appoints the management.* • *Boards are generally small (average of the ten largest listed companies is 6.6) and evidence has shown that smaller boards tend to perform better, provided that they have the necessary mix of skills and support (e.g., corporate secretary) – as it seems to be the case in Latvia.* • *Legal entities cannot serve as board members.* • *Only in banks there are qualification requirements for board members. In companies, this is recommended by the Corporate Governance Principles.* • *Public interest entities are required to have an audit committee, with at least one independent member with financial education and experience. The Principles recommend that that at least three of the audit committee's members have adequate knowledge in accounting and financial reporting. Executives cannot be committee's members. Nine among the ten largest listed companies declared having an audit committee in place.* • *Systemically important banks are also required to have other committees in place.* • *The Principles recommend that companies have at least half of the board made by independent board members. Five out of the ten largest companies disclose having independent board members (however, only in three cases, they represent the majority of the board).* ***Weaknesses:*** • *The audit committee is not necessarily a board committee: it is appointed by the general shareholders meeting and can include "outsiders" (i.e., non-board members). In particular, the independent member of the audit committee cannot be a board member. We are not convinced this is the right solution (see comments below).*
1.2. Gender Diversity at the Board (20.45%) *Moderately Strong*	• *All ten largest listed companies disclose the composition of their boards.* • *It appears that six out of the ten largest listed companies disclosed having women on their boards: four women in one company; three in three companies (in one case, they are majority of the board) and two women in two companies (average in these boards: 34.1%).* • *In total, there are 15 women among 66 board members in the ten largest listed companies with an average of female representation in boards of 20.45 per cent.*
1.3. Independent Directors *Fair*	***Strengths:*** • *The Principles recommend that at least half of the board is made by independent members.* • *Public interest entities are required to have an audit committee, where at least a member is independent.* • *Five out of the ten largest companies disclose having independent board members, however, only in three cases, they represent the majority of the board. The other five companies disclose in their "comply or explain" reports that they do not have independent members on the board.* ***Weaknesses:*** • *There are at least two definitions of independence: one in the Principles, which refers to board members and one*

Key Areas and Rating	Strengths and Weaknesses
	in the Law on the Financial Instruments Market which refers to audit committee members. Two definitions might cause confusion. Neither definition includes any "positive criteria" (i.e., what an independent directors is expected to do in practice). It should be pointed out that the concepts of "non-affiliation" and "independence" are different. While non-affiliation can be established by negative criteria, independence necessarily needs objectivity of mind and character, which is a positive characteristic that should be demonstrated, disclosed and explained in practice.
1.4. Board Effectiveness *Weak*	***Weaknesses:*** • *In companies, the law does not explicitly empower the board to approve the company's budget, strategy and risk profile. The Principles recommends that these functions should be undertaken by the board. However, the law for banks is more precise in this respect.* • *There is no established practice of board evaluation. No company disclose undertaking this exercise.* • *The law does not require and the Principles do not recommend companies to have a corporate secretary. We could not find any information on corporate secretary positions disclosed by the companies, therefore we cannot confirm if companies have created such a position. We believe the corporate secretary is essential in order to ensure that boards perform effectively.* • *It was not possible to assess the activities of board and committees, as this information is not disclosed.*
1.5. Responsibilities of the Board *Fair*	***Strengths:*** • *Fiduciary duties, liability of board members and conflicts of interest are regulated by law, and elaborated quite extensively in the case law and judicial practice (for further details, see: http://ec.europa.eu/internal_market/company/docs/board/2013-study-reports_en.pdf)* ***Weaknesses:*** • *As mentioned above, the law does not clearly confer to the board of companies some of its key functions.*

Key Areas and Rating	Strengths and Weaknesses
2. Transparency and Disclosure *Moderately strong*	*Disclosure requirements are detailed in the law and appear to be generally well implemented. However, information on beneficial ownership, board's activities and audit committee's activities and meetings is not systematically disclosed.* *The law requires companies to prepare and disclose their financial information in line with IFRS, and all ten largest listed companies appear to comply with this requirement.* *The law details the disclosure requirement to the market and to shareholders. The law appears to be well implemented, also thanks to the Official Storage System, a publicly available internet portal, which includes information on the general shareholders' meeting.* *Listed companies are also required by law to disclose their compliance with the Principles (under the "comply or explain" approach") and it appears that all ten largest listed companies included a corporate governance statement in their annual reports, with explanations in case of non-compliance. Explanations are often meaningful, but sometimes there are some clear misunderstandings of the Principles.* *Companies are required to disclose detailed information on the external auditor, and auditors are required to make a yearly declaration of independence to the audit committee. Companies appear to comply with the requirements of the law, however some doubts arise with reference to rotation of auditors and provision of non-auditing services.* *Companies do not appear to have codes of ethics in place.*
2.1. Non-Financial Information Disclosure *Moderately strong*	***Strengths:*** • *All ten largest listed companies provide some information about their strategy in their annual reports or websites.* • *All companies and banks are required by law to prepare and publish an annual report, including detailed non-financial information. All ten largest listed companies appear to comply with this requirement, however, non-financial information is often limited (e.g., audit committee's meetings and activities).* • *On average, the websites of the ten largest listed companies are informative, well updated and relatively easy to find. Sometimes the information is incomplete.* • *The law requires listed companies to report their compliance with the Corporate Governance Principles. All ten largest listed companies appear to comply with this requirement.* • *The Corporate Governance Principles recommend listed companies to post their Articles on the website and the large majority of the ten largest listed companies comply with this recommendation.* • *Listed companies are required to disclose information on board composition and qualification of members. All ten largest listed companies disclose the names of their directors and eight of them disclose their qualifications as well.* • *All companies provide up to date information on their shares and capital on their own websites.* • *The Official Storage System is publicly available internet portal, which includes information on the general shareholders' meeting.* ***Weaknesses:*** • *Information on audit committee's composition, qualification of members, activities and meetings is limited.* • *All ten largest listed companies disclose information on their shareholders; but only three of them seem to go into details and disclose their main beneficial owners as well.* • *None among the ten largest listed companies disclose having a code of ethics in place.* • *Disclosure on transaction in company shares by board members and executives appear to be limited.*
2.2. Financial Information Disclosure *Strong*	***Strengths:*** • *Since 2005, companies and banks are required to prepare and disclose their financial statements in line with IFRS and all ten largest listed companies appear to comply with this requirement*
2.3. Reporting to the Market and to Shareholders *Strong*	***Strengths:*** • *All ten largest listed companies post their annual reports on their websites. Annual reports are also available at the Official Storage System.* • *The minutes of the general shareholders' meeting of all ten largest listed companies are available ether on their websites or on the stock exchange website and on the Official Storage System.* • *The law requires companies to disclose price sensitive information.*

Key Areas and Rating	Strengths and Weaknesses
2.4. Disclosure on the External Audit *Moderately strong*	***Strengths:*** • *Companies are required to disclose detailed information on the external auditor, and auditors are required to make a yearly declaration of independence to the audit committees of audited entities. All ten largest listed companies disclose the name of their external auditors. Nine of them are international audit firms.* • *The authority to appoint the audit is assigned to the general shareholders meeting, upon proposal by the audit committee.* • *The law requires the external auditor to be independent and the audit committee is in charge of monitoring its independence.* • *The large majority of the ten largest listed companies have an audit committee in place.* ***Weaknesses:*** • *Provision of non-audited services by the external auditor is allowed under the scrutiny of the audit committee. Disclosure on this matter is extremely limited.* • *Rotation of external auditor is required after seven years. However, it seems that at least four of the ten largest listed companies have not rotated their auditors in the last 9-10 years.*

Key Areas and Rating	Strengths and Weaknesses
3. Internal Control *Fair*	*Banks are required to create internal audit and compliance functions. Other companies might appoint an internal audit and/or a company controller, but these functions are created upon shareholders' request and are different from what is generally understood as internal audit.* *Public interest companies must establish an audit committee, but it is not necessarily a board committee, as it can include "outsiders" (i.e., non board members), a common practice in Latvia. We do not think this is ideal.* *External auditors are required to be independent, but they are allowed to provide non-auditing services. Rotation of external auditors is required, but this requirement does not seem to be well implemented.* *None of the ten largest listed companies disclose having codes of ethics in place.* *Whistleblowing legislation is not comprehensive.* *Related party transactions and conflicts of interest are regulated by law. The competence to approve related party transactions is assigned to the board and in some cases to the general shareholders' meeting. There is no requirement for the audit committee to review related party transactions.*
3.1. Quality of the Internal Control Framework *Fair*	***Strengths:*** • *All ten largest listed companies disclosed having appointed an external auditor (nine are international audit firms) and established an audit committee. Six have an internal audit function in place.* • *Banks are required to establish an internal audit function and a standalone compliance function.* • *In banks, the function of the internal audit can be delegated to an external auditor (however not the same that is auditing the bank).* ***Weaknesses:*** • *There is no requirement for the internal audit to report to the audit committee.* • *Public interest entities must establish an audit committee, but it is not necessarily a board committee* • *None of the ten largest listed companies disclose having codes of ethics in place* • *There is no comprehensive whistleblowing legislation.*
3.2. Quality of Internal and External Audit *Fair*	***Strengths:*** • *The audit committee is in charge of monitoring the independence of the external auditor.* ***Weaknesses:*** • *Internal audit is required only for banks.* • *By law, the reporting line of the internal audit function is to the board. Because public interest entities are required to have an audit committee, it would make sense to require the internal auditor to report to the board via the audit committee.* • *External auditors are required to be independent, but they are allowed to provide non-auditing services under the scrutiny of the audit committee) No company discloses the provision of non-auditing services by the external auditor or any consideration by the audit committee on this matter.* • *Rotation of external auditors is required, but the law does not seem to be well implemented.*
3.3. Functioning and Independence of the Audit Committee *Fair*	***Strengths:*** • *Public interest entities are required to establish audit committees and nine out of the ten largest listed companies disclose having established one.* • *Executives are not allowed to be members of the audit committee.* ***Weaknesses:*** • *The audit committee is not necessarily a board committee: it is appointed by and accountable to the general shareholders meeting (see Section 12 of the Corporate Governance Principles) and can be composed of outsiders (i.e., non-board members). This is a common practice in a number of countries, but we are not convinced this is the right solution, especially when the functions delegated to the committee are typical board functions. We think instead that it is essential that audit committee members who are recommending specific actions to the (supervisory) board are then able to follow up on them when they are discussed and voted at the board. This would reinforce their positions and the board's 'objective judgement' – to the extent that, of course, those sitting in the audit committee are truly independent and qualified board members. Further, we believe that committees' members should have a thorough understanding of the corporation's business when performing their duties, while 'outsiders' – as they do not sit at the board – might only have a partial vision and understanding of the corporation's activities. While it is legitimate that committees might need external advice or expertise on specific issues, they should be able to request such advice but without allowing outsiders to take the place of board*

Key Areas and Rating	Strengths and Weaknesses
	members in their determinations. Finally, committees that include outsiders might have confidentiality and accountability issues, since outsiders might not be bound by the same duties of loyalty and care required from board members. The key question here is what could a person that it is not a board member add to the debate? The discussion is open. Our opinion is that the structure might be more effective if the board includes some independent non-executive members who would also sit on committees, instead of outsiders. • *Nine among the ten largest listed companies disclosed having and audit committee, but only three (all banks) disclose its composition and in all cases it appears that the audit committee is composed by a majority of non-board members.* • *It is not clear why the law requires that the independent member of the audit committee cannot be a (supervisory) board member.* • *There is little or no information disclosed on audit committees' meetings and activities provided by the ten largest listed companies*
3.4. Control over Related Party Transactions and Conflict of Interest *Moderately strong*	***Strengths*** • *The law defines related parties and the procedure for approving related party transactions. The definition of related party transactions is consistent with IFRS.* • *Banks are required to develop a policy on the management of conflict of interests.* • *The competence to approve related party transactions is assigned to the board and in some cases to the general shareholders meeting.* • *All ten largest listed companies disclose related party transactions within the notes to the financial statements or in the annual reports.* ***Weaknesses*** • *There is no requirement for the (independent) audit committee to review related party transactions.* • *We have found no evidence of enforcement over these matters.*

Key Areas and Rating	Strengths and Weaknesses
4. Rights of Shareholders *Moderately Strong*	*Basic shareholders rights are granted by law and generally well implemented.* *Minority shareholders can call a general shareholders meeting (GSM), nominate board members, request cumulative voting and start a derivative suit. Major corporate changes require qualified majority. However, pre-emptive rights can be waived by simple majority.* *Insider trading and self dealing are regulated by law, which appears to be well enforced.* *Regulation on minority shareholders protection and shareholders' access to information seem to be comprehensive and generally in line with best practices. Explanations provided in the "comply or explain" reports are generally meaningful.* *Share register for listed companies is maintained by an independent registry institution.* *Shareholders agreements must be disclosed; however, they are rarely used and not much regulated. They are generally considered to be enforceable between the parties, however there is no consolidated case law on the matter.*
4.1. General Shareholders' Meeting (GSM) *Moderately strong*	***Strengths:*** • *Shareholders representing 5% of the shares can call a GSM and can propose new items to the GSM agenda.* • *Shareholders representing 5% of the shares can nominate board members and request to have cumulative voting.* • *By law, notification with the agenda of the GSM needs to be sent to the shareholders at least 30 calendar days before the meeting.* • *Disclosure on GSM documentation is available on the Official Storage System and at https://csri.investinfo.lv* • *Shares carry voting rights in proportion to their value.* ***Weaknesses:*** • *Disclosure on voting rights and their exercise by shareholders is limited.*
4.2. Protection against Insider Trading and Self-dealing *Moderately strong*	***Strengths:*** • *Insider trading is regulated and prohibited by law and appear to be well enforced in practice.* • *Related party transactions are regulated by law.* • *All ten largest listed companies disclose related party transactions within the notes to the financial statements.* ***Weaknesses:*** • *The regulation on self-dealing does not provide for an appraisal by an independent evaluator to establish if the price paid is fair or equal to market value. The audit committee is not required by law to be involved in the analysis and approval of related party transactions.*
4.3. Minority Shareholders Protection and Shareholders' Access to Information *Moderately strong*	***Strengths:*** • *All ten largest listed companies publish their annual reports on their websites and stock exchange website (http://www.nasdaqomxbaltic.com/market/?lang=en).* • *Shareholders enjoy pre-emptive rights in all cases of capital increase, however a waiver can be granted by simple majority of votes by the GSM.* • *Major corporate changes must be approved with a supermajority vote at the GSM (the blocking minority shareholding for major corporate changes is 25%+1). However (as mentioned above) pre-emptive rights can be waived by simple majority.* • *Shareholders with 5% shares can start a derivative suit.* ***Weaknesses:*** • *Non-financial information include in the annual reports is sometimes limited and incomplete.* • *The necessary majority for waiving pre-emptive rights should be increased.*
4.4. Registration of Shareholdings *Moderately strong*	***Strengths:*** • *Registration of shareholding by an independent registry (Latvian Central Depositary) is required by law.* • *Significant shareholding variations must be disclosed to the company.* • *In listed companies, shareholders agreements concerning voting rights which are known by the company must be disclosed.* ***Weaknesses:*** • *Shareholders agreements are rarely used and not much regulated. They are generally considered to be enforceable between the parties, however there is no consolidated case law on the matter.*

Key Areas and Rating	Strengths and Weaknesses
5. Stakeholders and Institutions *Fair/Moderately strong*	*The stock exchange appears to have limited capitalisation and liquidity, but it is active in promoting good quality disclosure by listed companies.* *International law firms and audit firms have material presence in the country, but presence of rating agencies is limited.* *The Corporate Governance Principles appear to be comprehensive, regularly reviewed and relatively well implemented. However, their implementation does not seem to be actively monitored.* *It appears that the institutional framework supporting good corporate governance is generally sound. This is also confirmed by international organisations indicators.* *The only negative note appearing from the assessment – common to a number of countries – is the limited attention paid by listed companies to queries of potential investors and stakeholders, which might be a sign of the need to develop better investor relation departments of issuers.*
5.1. Corporate Governance Structure and Institutions *Fair/Moderately strong*	***Strengths:*** • *The Stock exchange (Nasdaq Riga) website includes a dedicated page on issuers (http://www.nasdaqbaltic.com/market/?pg=issuers&lang=en) with general information and contact information, financial reports, announcements, and fact sheet for each issuer. The stock exchange appears active in promoting good quality disclosure by listed companies.* • *The market regulator is the Financial and Capital Market Commission, which carries out the supervision of Latvian banks, credit unions, insurance companies and insurance brokerage companies, participants of financial instruments market, as well as private pension funds, payment institutions and electronic money institutions. The website of the Commission provides information on supervised entities and legislation in force.* • *International audit and law firms have a material presence in the country.* ***Weaknesses:*** • *The stock exchange has limited capitalisation and liquidity.* • *There is no listing segment requiring listed companies to have significantly higher corporate governance standards than those required for other listed companies.* • *International rating agencies are not active in the country.* • *There are limited corporate governance training providers in the country.*
5.2. Corporate Governance Code *Fair*	***Strengths:*** • *The Corporate Governance Principles have been adopted in 2005 and reviewed in 2008 and 2010.* • *The Principles refer to the OECD Corporate Governance Principles and consist of six main chapters, dealing with (i) shareholders' meeting; (ii) board; (iii) council; (iv) disclosure of information; (v) internal control and risk management; (vi) remuneration policy. In the Principles' Annex the independence criteria of supervisory council members are defined.* • *Listed companies are required to report on their compliance with the Principles (so-called "comply or explain"). All ten largest listed companies disclose how they comply with the Principles. Explanations are often meaningful, but sometimes there are some clear misunderstandings of the Principles or reluctance to comply with them.* ***Weaknesses:*** • *It appears that there is no body actively monitoring how the Principles are implemented in practice (no report on this matter is published).* • *We have no evidence of courts referring to the Principles as a source of obligations or rights.*
5.3. Institutional Environment *Moderately strong*	***Strengths:*** • *It appears that there are only limited inconsistencies between laws and regulations in corporate governance matters.* • *Case law collections appear easily accessible by lawyers in the country, however collections are not aggregated in a timely manner.* • *Indicators by international organisations show a sound framework, among the best in the EBRD region.* ***Weaknesses:*** • *It appears that there is little attention by the largest listed companies to queries by stakeholders, which might be a sign of the need to develop better investor relation departments of issuers.*