

New insolvency and bankruptcy regulations in Latvian mortgage bond legislation

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Mortgage and Land Bank of Latvia

8th Central European Covered Bond Conference

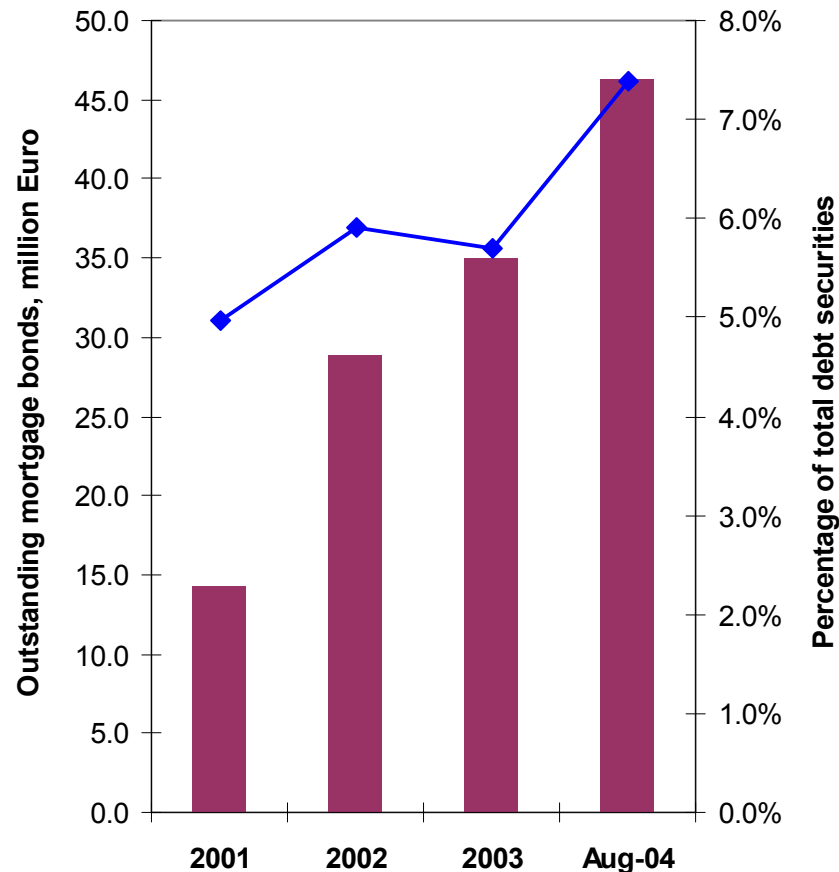
Copenhagen, 18-19 October 2004

Covered bond model in Latvia



- Universal bank with the qualified mortgage bond license
- Qualified requirements for issuing mortgage bonds
 - minimum equity requirement (LVL 5 million)
 - no restriction to provide financial services
 - internal regulations (valuation & cover)

Mortgage bond market



- One issuer – Mortgage and Land Bank of Latvia (issuing since 1999)
- Mortgage loans as percentage of GDP
 - 7.9% in 2002
 - 13.7% in 2003
- Outstanding mortgage bonds as percentage of GDP
 - 0.3% in 2002
 - 0.4% in 2003

Law on Mortgage Bonds

- Approved in 1998
- Amended in:
 - 2000 - increase of LTV ratio from 60% to 75% for residential mortgage loans
 - 2001 - unified supervision of the financial markets (Financial and Capital Market Commission)
 - 2002 - introduction of new insolvency and bankruptcy regulations and mandatory over-collateralization as well as strengthening ALM

Levels of the insolvency and bankruptcy regulations

Suspension / losing the rights
to issue mortgage bonds

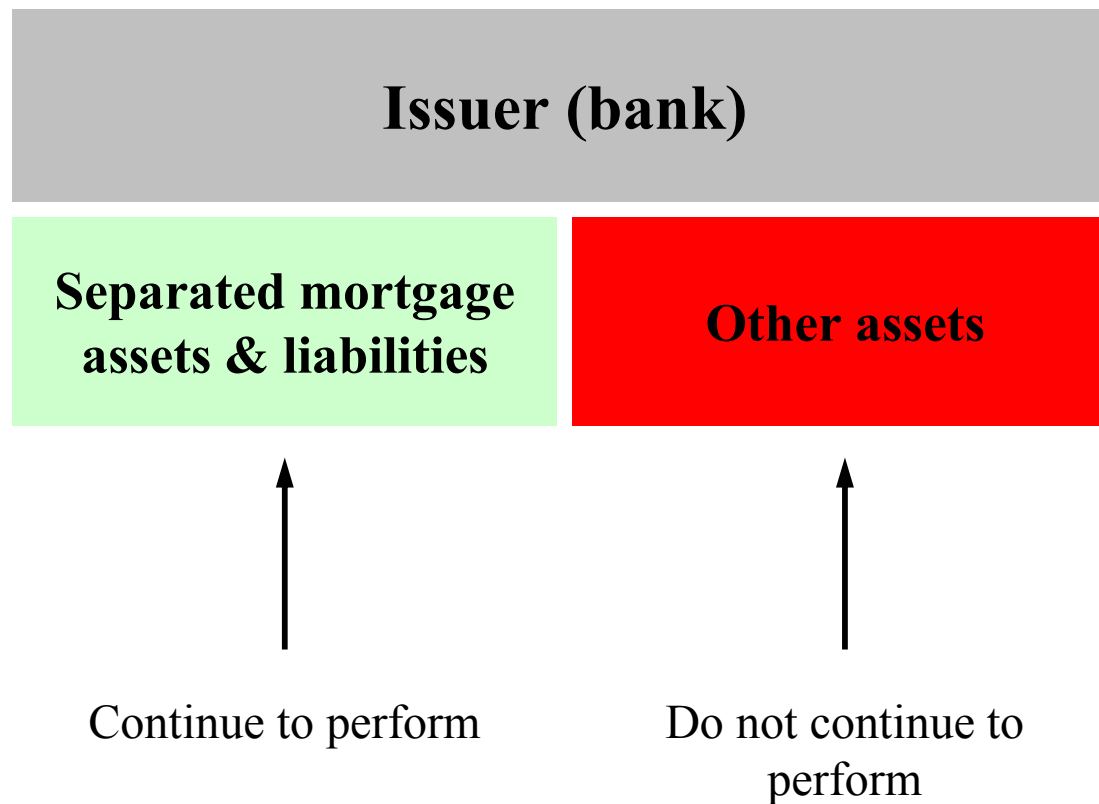
Insolvency and bankruptcy of
an issuer

Insolvency and bankruptcy of
a mortgage bond cover

Suspension / losing the rights to issue mortgage bonds

- Inconsistency with the requirements for an issuer defined by the law, “mortgage bond cover assets < outstanding mortgage bonds”, mismatching of maturities / currencies or over-collateralization lower than mandatory minimum are the reason for suspension / losing rights to issue mortgage bonds
- Issuer has to take all necessary actions to eliminate discrepancies or to renew the mortgage bond cover
- Forbidden to register new mortgage bond issues or to place already registered mortgage bond issues
- No changes to the structure of the mortgage bond cover are allowed

Insolvency and bankruptcy of an issuer



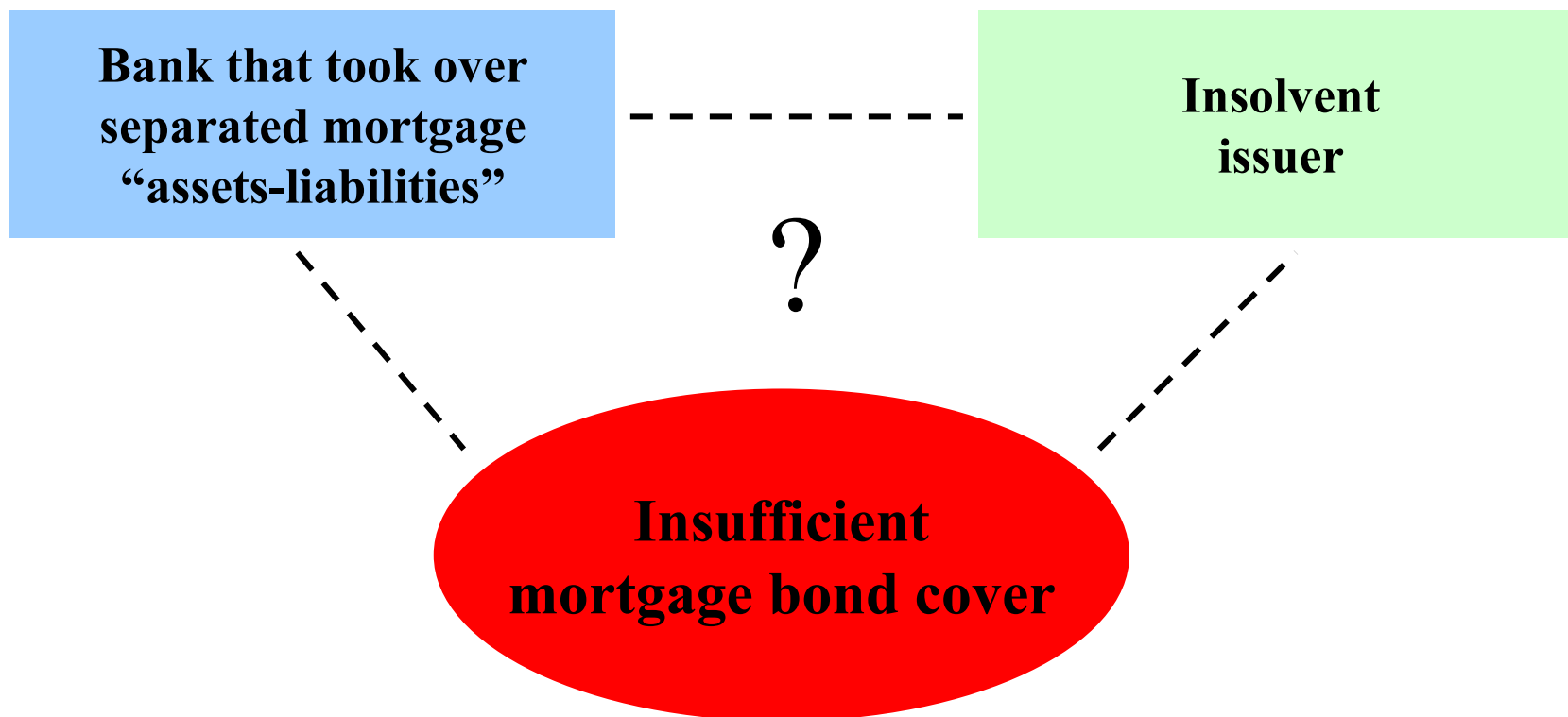
Insolvency and bankruptcy of an issuer (1)

- One insolvency administrator appointed by the court
- Transfer of assets included in the mortgage bond cover and liabilities arising from outstanding mortgage bonds to another bank within a specified period of time
- Segregation of the mortgage bond cover
 - separate management of the assets and their proceeds until transfer to another bank
- No changes to the structure of the mortgage bond cover are allowed

Insolvency and bankruptcy of an issuer (2)

- Limited use of proceeds from the assets included in the mortgage bond cover before transferring “assets-liabilities”:
 - regular interest and principal payments to mortgage bond holders and counterparty under the cover assets hedge contract
 - purchase of mortgage bonds on the secondary market and immediate redemption
- Transfer of the voluntary over-collateralization by the take-over bank to the insolvent issuer

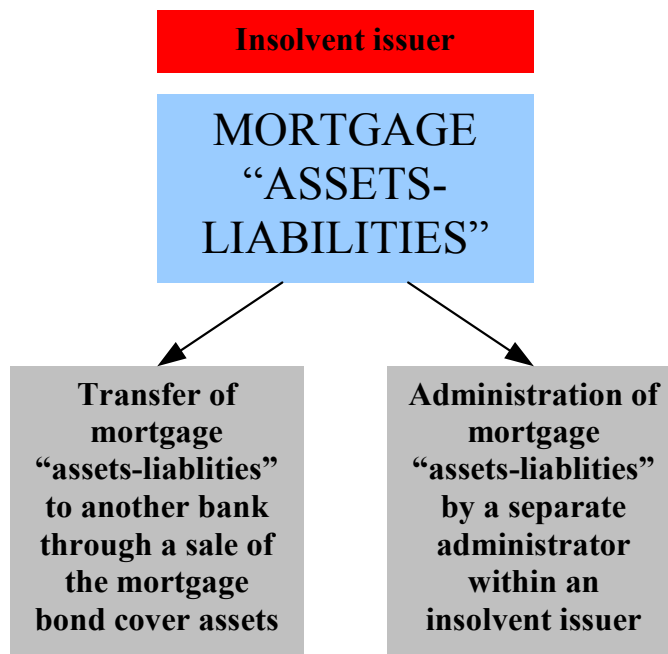
Insolvency and bankruptcy of the mortgage bond cover



Insolvency and bankruptcy of the mortgage bond cover

- If a bank that takes over mortgage “assets-liabilities” can not provide sufficient mortgage bond cover, for example, mandatory over-collateralization is lost, the FCMC requests to declare the mortgage bond cover insolvent
- All mortgage bond holders have the same rank in case of insolvency / bankruptcy of the mortgage bond cover
- Until proceeds from the mortgage bond cover meet claims from the outstanding mortgage bonds, mortgage bonds do not accelerate
- If the claims of mortgage bond holders can not be fully satisfied during the insolvency procedure of the mortgage bond cover, the mortgage bond cover is declared bankrupt and mortgage bonds accelerate

Legislative improvements to the insolvency and bankruptcy regulations



- Clarification as regards the practical implementation of the alternatives in case of the insolvency / bankruptcy of an issuer and the mortgage bond cover
 - transfer of separated mortgage “assets-liabilities” to other bank (“full responsibility” or “administrative functions”)
 - separate administration of the mortgage bond cover within a structure of an insolvent issuer by a separate insolvency administrator
- Permission to make changes to the mortgage bond cover in order to renew the sufficiency of the mortgage bond cover in case of suspension or losing rights to issue mortgage bonds

Overview on the insolvency and bankruptcy regulations

	Suspension / losing the rights to issue mortgage bonds	Insolvency and bankruptcy of an issuer	Insolvency of a cover	Bankruptcy of a cover
Fulfillment of requirement that cover assets exceed mortgage bonds	Yes	Yes	No	No
Fulfillment of requirement of matching maturity & currency of the cover assets and mortgage bonds	Yes	Yes	No	No
Fulfillment of requirement of the minimum mandatory over-collateralization	Yes	Yes	No	No
Fulfillment of requirement of the maximum substitute cover	No	No	No	No
Does the minimum mandatory over-collateralization stay with the cover?	Yes	Yes	Partly, yes	No
Are changes to the structure of the cover allowed?	Not allowed	Not allowed	Not allowed	Not allowed
Does the voluntary over-collateralization stay with the cover?	Yes	No	No	No
Is there bankruptcy segregation?	N/a	Yes	Yes	Yes
Are mortgage bonds accelerating?	No	No	No	Yes