UPCOMING AMENDMENTS TO FINANCIAL REGULATION

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Amandments to the Commercial Law

Upon the request of the Riga Stock Exchange, the Finance and Capital Markets Commission has drafted amendments to the Commercial Law. The aim of the amendments is to eliminate controversies between the Commercial Law and the Financial Instruments Markets Law (FIML) regarding listed joint stock companies and their relations with shareholders.

Firstly, the amendments prescribe that it will be possible to publicly trade only registered shares. Bearer shares will have to be in a paper form. These amendments ensure that the issuers possess all information regarding their shareholders in order to guarantee investor protection, to prevent abuse of insider information and to prevent market manipulations. They also simplify banks' and investment broker companies' procedures for identifying clients.

Currently the Commercial Law states that a person obtains all of a shareholder's rights from the moment this person is entered in the company's shareholder register. According to the FIML, the financial instruments belong to their acquirer from the moment book entries, in respect of those financial instruments, are made in the financial instruments account of the acquirer.

To eliminate this controversy, the amendments prescribe that rights stemming from publicly traded shares must be determined in accordance with the FIML. Also the registration of these shares will be regulated by the FIML. Among other things, the amendments provide the possibility to all joint stock companies to entrust the registration of their shareholders to the Latvian Central Depositary.

Furthermore, many joint stock companies whose shares are publicly traded have experienced that, in practice, it is not possible to comply with the rules of the Commercial Law regulating order in which the shareholder meetings of joint stock companies shall be convened. The problem arises because, according to the Commercial Law, the joint stock company shall inform all its registered shareholders 30 days before the shareholders' meeting.

However, according to the regulations of Latvian Central Depositary, the shareholders possessing publicly traded shares must submit to their banks an order to block the shares in the financial instruments account only 10 days before the shareholders' meeting. Thus the shares can be traded up to the tenth day before the shareholders' meeting. As a result, the company cannot inform all its shareholders as prescribed by the Commercial Law. Due to this, the amendments provide that the joint stock company shall inform its shareholders through the stock exchange in which its shares are traded.

The amendments also clarify the rules of the Commercial Law by providing that the rights to dispose publicly traded shares cannot be restricted. In addition, the amendments provide that in case of a public offer, when the shares are publicly traded, the term for exercise of pre-emption rights to newly issued shares can be reduced to one week (the general term is one month).

It remains to be seen when and in what wording these amendments will be passed by the Latvian parliament (*Saeima*). However, the market participants already have expressed their support for the amendments considering that the controversies described above affect and burden the everyday life of listed joint stock companies.

Mifid in Latvia

On May 23 2007 the Latvian government approved substantial amendments to the FIML. The precise date the amendment will passed by the Latvian parliament and will become effective is not yet known. By these amendments Latvia will implement the Markets in Financial Instruments Directive (Mifid).

Aim of Mifid

Mifid replaces the Investment Services Directive. Member states have had to transpose and implement Mifid in their national legislation by January 31 2007, but they will only apply these measures from November 1 2007.

Mifid extends the coverage of the Investment Services Directive and introduces new and more extensive requirements that firms will have to adapt to, in particular for their conduct of business and internal organization. Therefore, at the end of this year the regulatory framework for investment firms will change significantly to reflect developments in financial services and markets.

Mifid aims to harmonize market conditions in financial instruments and the operation of investment firms. However, it leaves the regulation of many issues at the discretion of the member states

Scope of regulation

Latvia has decided not to include undertakings other than legal entities in the definition of investment firms. Furthermore, under Article 3 of Mifid, Latvia has decided to provide exemption from the regulations only to companies providing investment services to their board and supervisory board members and employees, as well as those in the same group of companies. This means that advisers and arrangers, which do not hold client money, will be subject to the requirements of the new rules.

Tied agents and eligible counterparties

The draft provides that investment firms will be allowed to appoint tied agents. However, they will not be permitted to handle clients' money or financial instruments. The draft also obliges the investment firms to verify whether tied agents are of sufficient good repute and have appropriate knowledge. For that purpose investment firms are required to keep a register of tied agents and make it publicly available on its web page. The register must be correct and up to date, and has *prima facie* credibility.

According to the current draft, only those undertakings that are enumerated in Article 24(2) of Mifid will be recognized in Latvia as eligible counterparties.

Under the current draft of the amendments to the FIML no requirements in addition to Mifid are imposed on investment firms. There are also no national requirements or restrictions to the marketing of particular financial instruments over and above the requirements of Mifid. As a result of the amendments to the FIML, competition among security market operators in Latvia should increase as it will be possible to introduce a multilateral trading facility.