The Treasury of the Republic of Latvia

Public Report for

2007

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Abbreviations used in the Report

CSB	Central Statistical Bureau
ECB	European Central Bank
EIB	European Investment Bank
eKase	Electronic settlement system of the government budget
ECDB	Council of European Development Bank
EBRD	European Bank for Reconstruction and Development
EU	European Union
EUROSTAT	European Union Statistical Bureau
GDP	Gross Domestic Product
Phare	The main instrument of financial and technical collaboration of the European Union with the Central and Eastern European countries
POS terminal	Electronic device automatically reading data from the magnetic strip or the smart card, sends request for authorisation to the transaction processing centre, receives an authorisation reply and stores the data of transactions.
PPP	Public-Private partnership
SAP	Government budget planning and execution information system
SAPARD	European Union pre-accession financial instrument, provided as Special Action Programme for Agriculture and Rural Development in Central and Eastern European countries
Strategy	Operational Strategy of the Treasury for 2007-2009 (updated for 2008-2010)
IMF	International Monetary Fund
TARGET 2	Trans-European Automated Real-time Gross settlement Express Transfer System
SRS	State Revenue Service
SSIA	State Social Insurance Agency
NIB	Nordic Investment Bank

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Contents

The Treasurer's Statement 4

Retrospect of the Treasury's History 5

Operational Strategy of the Treasury 6

Legal status and structure of the Treasury 8

The Treasury's Operation in 2007:

1. **Central government budget execution** 10
   - 1.1. Organizing of central government budget execution for 2007 10
   - 1.2. Accounting and reporting 11
   - 1.3. Electronic services development 13
   - 1.4. Concept of development of services provided by the Treasury's settlement centres 14
2. **Central government debt, cash and budget loan management** 15
   - 2.1. Central Government Debt Management Strategy 16
   - 2.2. Changes in central government debt in 2007 16
   - 2.3. Central government domestic debt 18
   - 2.4. Central government foreign debt 18
   - 2.5. Management of government borrowing 18
   - 2.6. Central government debt portfolio management 19
   - 2.7. Central government loans 19
   - 2.8. State guarantees 20
   - 2.9. Liquidity management 20
   - 2.10. Facilitating public-private partnership 21
3. **Implementation of the functions of the Paying and Certifying Authority for the European Union policy instruments** 22
   - 3.1. Function of the Paying Authority 22
   - 3.2. Function of the Certification Authority during the planning period from 2007 to 2013 24
4. **State-funded pension scheme asset management** 25
5. **Corporate governance of the Treasury as a public administration institution** 26
   - 5.1. The Treasury's financing and its spending 26
   - 5.2. Personnel and personnel management 30
   - 5.3. Quality and risk management 31
   - 5.4. Internal control system 32
   - 5.5. Information technology development 32

Public communication 33

Treasury's development priorities for 2008 34

The Treasurer's Statement

2007 was a significant year for the Treasury with many essential and relevant events.

The Treasury's activities still comply with the best management principles and are attested by the external supervisory audit performed in the Treasury, which confirmed that the Treasury maintains its management system in accordance with the requirements of ISO 9001:2000 Quality management system and implements specified policies and goals, and by a confession letter received within the framework of the *Annual Efficient Management Prize 2007*. Taking into account the principles of unitary operation of the institution specified within the Strategy and the principles of collaboration defined within the Client Service Manual, an atmosphere has been created in the Treasury that facilitates work and collaboration.

For the convenience of our clients and cooperation partners, we implement ever-new services and solutions in the execution of entrusted functions. We have collaborated with "Hansabanka" AS since 2007 to provide servicing of credit cards attached to the Treasury's accounts for government budget institutions and, at the end of year, implemented the direct participation of the Treasury in the Trans-European Automated Real-time Gross settlement Express Transfer system, TARGET2.

The Treasury's activities were significantly influenced by sharp changes in the local and international financial market. Emphasis should be mainly put upon the developmental tendencies of the macroeconomic situation in Latvia, which were paid special attention not only by credit rating agencies, but also by foreign investors. As a result, the Treasury needed to change the loan measures it had planned – to reduce sales of domestic loan securities and temporarily transfer planned Eurobond issuances.

In order to improve the management of the temporarily available financial resources from the government's budget, we have provided preparatory measures within the framework of the Cash Management Strategy for security transactions and have expanded the circle of our business partners by attracting both local and foreign institutions operating in financial asset investments. We have commenced implementation of the market value risk assessment model Value-at-Risk, providing the opportunity to determine potential losses from a specific security portfolio, and which is one of the analysis tools used to make decisions regarding the purchase of a respective security at a specific moment in time.

In order to expand the range of financial instruments within the framework of central government debt management and cash management, we commenced implementation of optional deal opportunities: in 2007, option assessment calculators were developed in whose calculations it is possible to apply methods to determine the price fluctuations of various financial instruments.

For the 2007-2013 planning period, we began the execution of functions of EU policy instrument certifying bodies and paying authorities for the following EU policy instruments: the European Regional Development Fund, the European Social Fund and the Cohesion Fund. We are responsible for the performance of the above-mentioned policy instruments in accordance with the interests of the European Community, ensuring effective management and supervision of the instruments in compliance with EU Directives and guidelines.

In 2007, one of the most significant periods within the history of operation of the institution came to a conclusion – the management of the Treasury's 2nd pension level investment plan; since October, the plan has been in the hands of private management institutions. The efficiency of the Treasury's actions during the administration of this plan is attested by the fact that, in 2007, upon completing its operation, the plan had the second best result since its going into effect, in comparison to other conservative pension plans.

2008 will also be indicative of several significant events in the Treasury's activities: in compliance with pre-approved government loan plans, all the preparatory work for issue of Eurobonds is completed. In the near future, we plan to develop the basic management principles for the reserve fund provided in the government budget, as well as to execute the pre-conditions for the implementation of new financial instruments (options) in the management of government debt and assets. Our intention is to ensure the continual improvement of services provided by the Treasury, of information technologies, of quality management systems and personnel development.

Kaspars Āboliņš
The Treasurer

Retrospect of the Treasury's History

30 May 2007 marked 125 years since the birth of Voldemārs Miesiņš, the founder and first Treasurer of the Treasury of the Republic of Latvia.

"When the State of Latvia was proclaimed on 18 November 1918, **V.Miesiņš** was invited to organise and establish the Treasury of the Republic of Latvia, which commenced its operation in December, 1918. The first sums of money were received in the Treasury as a contribution from the German State Commissioner Vinings – three cheques, of 200 000 Ost Roubles each. The first domestic payment –from a student named Dukāts – a few thousand Roubles. The first tax was received from the Rūtenbergs' Tobacco Factory – 525 Ost Roubles. The first "inflow" of gold and foreign currency: a country woman donated two fivers and some English (war) ship officers exchanged the Czar's money for five or six British pounds. The first payment was received by Jāzeps Grosvalds – 300 Roubles", remembers V.Miesiņš' son-in-law, Georgs Lielbriedis.[1]

"When the Bolsheviks approached, all the valuable things from the Treasury were evacuated from Riga. V.Miesiņš transferred all of the State's "treasures" to the Minister of Finance K.Puriņš and his brother-in-law; they went to Liepāja. Miesiņš remained in Riga as manager of the bank's depositary. When the O.Kalpaks battalion and Landeswehr approached Riga, panic broke out among the Bolsheviks – the Treasury, as well as treasures received from citizens, were left in a strongroom in Riga. They sent Red Latvian Riflemen with trucks to "save" the money, however, none of them knew how to open the safe. They asked V.Miesiņš; he answered he did not know how, but he could try. V.Miesiņš intentionally put the key in upside down and, when it was pushed into the lock, it stuck - the strongroom could not be opened anymore. The money of Latvia and other valuable items were saved. The paymaster of the German occupation's Landeswehr oversaw the Treasury. After the Latvian Northern Army and Estonian victory at Cēsis, Kārlis Ulmanis travelled from Liepāja to Riga with the ship "Saratov", and the Treasury was taken over by the Latvians. Minister of Finance K.Puriņš and Director of the Board of the Treasury Vanags went to the National Opera, where V.Miesiņš was rehearsing (he was an opera singer), and invited him to undertake the position of organiser and manager of the Treasury."[2]

The official beginning of the Treasury's history can be dated on 25 March 1919, when the Prime Minister of the Republic of Latvia K.Ulmanis and the Minister of Finance K.Puriņš issued the decree on the system of the Treasury, and entrusted the execution of the budget to the Treasury.

During the time period from 1927 to 1928, the function of the budget cash department was performed by banks, but from 1928 to 1992 – the central bank.

The beginning of the modern Treasury is marked by the IMF technical relief mission, which in 1992 suggested establishing the Treasury as an independent institution, and the Ministry of Finance of the Republic of Latvia elaborates the operation model of the Treasury in collaboration with the IMF technical relief missions. The Council of Ministers made the decision (on 28 December 1992, No.557) to transfer the functions of the Treasury to the Ministry of Finance, establishing a gradual take-over of functions of the Bank of Latvia's cash department to ensure the accumulation of budget resources to finance expenditures, as well as to ensure a complete accounting of budget assets.

Since 1997, the Treasury has been an independent entity directly subordinate to the Ministry of Finance, which ensures the government budget execution and government debt management functions.

[1] G.L.Lielbriedis. 125 Anniversary of the Birth of First Treasurer of the Republic of Latvia, Voldemārs Miesiņš. "Laiks", May 26-June 1, 2007

[2] Ibidem

Operational Strategy of the Treasury

The Treasury's **main goal** is to develop as a dynamic and modern, client needs-oriented organisation with regard to the quality of its provided services, effectively and safely managing the finances entrusted to the Treasury's management according to the best financial management practices and in compliance with the interests of the Republic of Latvia and its people.

The Strategy sets the main operational principles, their strategic goals and tasks, as well as the budget programmes and sub-programmes with which they comply. Each programme and sub-programme of the budget involves a goal and resulting indicators, which the Treasury plans to achieve by development, making decisions regarding the execution of routine and long-term tasks and involving all Treasury staff in attaining the established objectives.

The Strategy sets the following **main operational directions** of the Treasury, which were executed during 2007 and are further explained in this report:

1) **Central government budget execution** aimed at economic management of the financial resources of the government budget, identification of the services required by the Treasury's clients, improvement of the quality of the provided services in line with the best international financial management practices and applying modern technologies;

2) **Central government debt management**, ensuring the financial resources required to execute financing of government budget and refinancing of the government debt at the lowest possible costs, hedging financial risks and taking into account the development of Latvia's capital market and financial system, as well as ensuring government financial interests during the process of rendering government-guarantee loans;

3) **Cash management and government budget lending**, ensuring effective and safe cash management, limiting financial risks, ensuring the liquidity required for execution of the government financial commitments on time and in full, as well as performing effective granting and servicing of government budget loans;

4) **Implementation of the Paying and Certifying Authority functions for the EU policy instruments** to ensure compliance with the financial management requirements prescribed by the EU and other allocating institutions, also applying them to the financial management of national financing, in order to ensure universal financial management standards for all finances assigned to the Treasury's management;

5) In 2007, one of the most significant periods in the operational history of the Treasury came to a conclusion – **management of the Treasury's 2nd pension level investment plan**. Since October, the plan has been transferred to private management institutions. Thus, in 2007, the Treasury completed its work in one of the main directions defined in the preceding years – management of the state-funded pension scheme assets, to ensure maximum safe investment of the funds assigned to its management and at the same time attain maximum income.

To achieve its strategic goals the Treasury observes unified **operational principles of the institution**:

1) quality and risk management;

2) personnel management;

3) an ensured, effective operation of the internal control system;

4) application of information technologies and security of information;

5) an ensured legitimacy and legal order.

The main priorities of the Strategy are:

1) **effective use of human resource capital** by promoting the development of all level staff and their involvement in the attainment of the Treasury's objectives;

2) **client-orientation** through identification of clients' needs and ensuring the availability of high-quality services using the latest developments in information technologies;

3) **streamlined and timely planning of the Treasury's finances**, in order to ensure spending efficiency of the Treasury's finances in compliance with set objectives;

4) **maximum effective use** of the benefits provided by **modern information processing technologies** to ensure the discharge of the Treasury's functions.

Legal status and structure of the Treasury

The Treasury is a direct administration institution subordinated to the Ministry of Finance. Its operational objective is the effective implementation of public administration functions in the area of public finance management.

The Treasury's operations are managed by **the Treasurer**. The Treasurer is appointed and dismissed from office by the Minister of Finance.

The Treasury has the following **functions**:

1) organising the execution and financial accounting of the central government budget;

2) give of assignations out and making payments from the central government budget revenue;

3) central government debt management;

4) management of the assets of the state-funded pension scheme (until 1 November, 2007);

5) functions of the Paying and Certifying Authority for the EU policy instruments, the Financial instrument of the European Economic Area and the bilateral Financial instrument of the Norwegian government established in laws and regulations and the National Fund functions delegated by the National Authorising Officer;

6) other functions prescribed by laws and regulations.

The legal status, functions, tasks, competence, rights and procedure for ensuring legality are stipulated by the Cabinet of Ministers Regulations No.677 **"Regulation of the Treasury"** issued on 3 August 2004 pursuant to the Public Administration Law.

The structure and work organisation of the Treasury is established by the Regulation of the Treasury issued on 1 August 2005, pursuant to the Public Administration Structure Law. In 2007, reorganisation of the structural units of the Treasury was carried out, changes in subordination of the structural units and in the competence of the structural units made, and amendments introduced to the Rules of the Regulation of the Treasury on 16 March and 4 October 2007.

In order to ensure good governance and optimise of the performance of the Treasury, adequate **changes** have been introduced **to the Treasury's structure** in 2007:

1) On 13 March 2007, direct subordination of the **Budget Execution and Monitoring Department** to the Deputy Treasurer on state budget accounting, reporting and transaction, as well as in issuing of reports and settlements, was established;

2) In November 2005, the Cabinet of Ministers issued a decree establishing that the Treasury's investment plan portfolio shall be transferred to private management institutions by organising a tender. During its September 2006 final reading , the Saeima adopted amendments to the State-Funded Pensions Law, providing the Treasury's operation in management of second level funds would be discontinued until 1 November 2007. As a result, the **State-funded pension assets management department** was liquidated on 2 January 2008.

In order to make unified decisions, the following **committees** continue their work in 2007:

Audit Committee – to improve the operation of the Treasury's internal control system, to facilitate the achievement of the Treasury's strategic goals, to protect its resources, and establish and maintain effective control of measures. The Committee reviews the findings and conclusions of internal and external auditors' reports on the Treasury's operations, recommendations included in the reports for operational improvements of the internal control system established in the Treasury, and comments provided by the audited structural units concerning the facts discovered during audits. The Committee is authorised to decide on potential measures for mitigation or prevention of the most significant Treasury's risks.

Central Government Debt Management Committee – to facilitate effective central government debt management and develop proposals for improvement and implementation of the Latvian Central Government Debt Management Strategy.

Credit Committee – to facilitate credit risk management by coordinating the activities of the Treasury's structural units concerning monitoring of the central government budget loans, guarantees issued on behalf of the government and counterparty limits.

Central Government Budget Accounting Committee – to update implementation of the financial accounting policy of the budget managed by the Treasury and ensure effective management of accounting policy changes. The task of the Committee is to define the accounting policy and its compliance with accounting standards, establish the accounting policy objectives, improve and update the accounting policy and facilitate compliance with the requirements established by the accounting policy.

Resource Liquidity Committee – to facilitate quality of cash management in order to ensure proper liquidity management in compliance with the tasks set in the Treasury's Cash Management Strategy.

Euro Changeover Committee – to draft proposals for ensuring the euro changeover in the areas of the Treasury's competence and coordinate the involvement of the Treasury's structural units in implementation of the relevant euro changeover measures.

Management Committee – to ensure effective management of the budget and personnel resources of the Treasury, attain the objectives set by the Strategy, and implement priority measures and new policy initiatives.

In 2007, **the Committee for Management of Information System Changes of the Treasury** was established to coordinate consideration and implementation of requests of the Treasury's Information System changes.

By consolidating the Quality Management System Monitoring **Committee and Risk Management Committee**, in 2007, the Quality and Risk Management Committee was established to facilitate constant improvement of the Treasury's operations and compliance of its services with the clients' needs, by ensuring effective quality, risk and information safety management.

Flowchart of the Treasury's Structure

Treasurer

- European Affairs Department
- State-funded pension assets management department
- Office
- Legal Department
- Internal Audit Department
- Quality and Risk Management Department
- Personnel Department
- Accounting Department
- Infrastructure Maintenance Department
- Treasury Units Coordination Department

Treasury Units (27)

(Aizkraukle, Alūksne, Balvi, Bauska, Cēsis, Daugavpils, Dobele, Gulbene, Jēkabpils, Jelgava, Jūrmala, Krāslava, Kuldīga, Liepāja, Limbaži, Ludza, Madona, Ogre, Preiļi, Rēzekne, Rīga, Saldus, Talsi, Tukums, Valka, Valmiera, Ventspils)

Deputy to the Treasurer on state budget execution and financial resource management questions

- Financial Resources Department
- Financing Department
- International Cooperation Department
- Financial Risk Management Department
- Forecasting and Financial Planning Department

Deputy to the Treasurer on state budget accounting, reporting, and transaction questions

- Reports Department
- Informatics Department
- Operations Department
- Budget Execution and Monitoring Department

The Treasury's Operation in 2007

1. Central Government Budget Execution

The Law on Budget and Financial Management has authorised the Treasury as the direct administration institution subordinated to the Ministry of Finance to organise the execution and the financial accounting of the central government budget and ensure granting of allocations and execution of payments made by budget institutions within the limits of the appropriations set in the annual central government budget.

While implementing the government budget, the Treasury maintains the State Budget Implementation System, where budget accounts for budget executors are opened; grants allocations based on financial plans; ensures payments of budget institutions by accepting both paper documents for payment execution as well as accepting instructions online via the *eKase*; keeps records of the budget execution transactions effected by institutions financed from the budget, monitoring their compliance with the annual appropriations from the government budget and keeps records of the government budget revenue as well as provides information concerning the collected taxes and fees to the State Revenue Service.

Ensuring uniform accounting of public finances, the Treasury drafts laws and regulations concerning the accounting in the central and local government budget institutions, thereby setting universal accounting principles, a universal chart of accounts and a reporting system, which is compliant with classifications approved by the Cabinet of Ministers and yields information on budget execution based on both the cash flow accounting principle and accruals principle. The uniform budget reporting system ensures aggregation of the reports submitted by central and local government budget institutions, and it is used not only by the Treasury, but also by the Ministry of Finance, State Audit Office, Bank of Latvia, Central Statistical Bureau and other public administration institutions.

1.1. Organizing of central government budget execution for 2007

In 2007, for the purpose of ensuring the central government budget execution, the Treasury granted **allocations in the amount of 4645.3 million lats**, of which 3661.9 million lats went to the basic budget and 983.4 million lats to the special budget. Allocations were granted to **640 budget institutions**, for which overall **3086 budget accounts were opened** (1568 accounts or 33.7% less than in 2006).

In comparison to 2006, the number of institution and basic budget accounts has decreased as a result of the Ministry of Regional Development and Local Government being named the executor of the programme 12.00.00 "Earmarked Subsidies for Activities by Local Government" (previously, the executor for the mentioned programme was not determined by the annual government budget law and a separate account was opened and allocations granted in compliance with a financing plan for each local government's activities) by the annual Law of the Government Budget.

In comparison with 2006, the number of the basic budget expenditure accounts in 2007 has decreased by 1524 accounts as:

1) since 2007, the procedure of accounting earmarked subsidies for local government activities was changed;

2) in 2007, reorganisation and merging of several State management institutions was performed, mainly in the areas of healthcare and agriculture (for instance, the merging of forest districts);

3) in 2007, a sharp decrease in the number of open accounts was

Table 1. **Number of central government budget income and expenditure accounts of the Treasury in 2006 and 2007**

Basic budget income accounts			Basic budget expenditure accounts			Special budget accounts (except grant and donation accounts)			Grant and donation accounts			Open current accounts: For local governments and their institutions			Open current accounts: For other budget-funded institutions		
2006	**2007**	%	2006	**2007**	%	2006	**2007**	%	2006	**2007**	%	2006	**2007**	%	2006	**2007**	%
285	289	1,4	4589	3065	-33,2	65	21	-67,7	304	309	1,6	1692	1832	8,3	1098	1211	10,3

observed, due to expenditure of the remaining pre-structural fund assets (Phare, SAPARD).

The decrease in the number of special budget accounts was influenced by the implementation of the centralised financial accounting system of the State Employment Agency (as of 2007, no separate accounts for each branch of the State Employment Agency have been opened).

In order to implement the government budget in 2007, the Treasury has elaborated the following laws and regulations:

1) Cabinet of Ministers 10 April 2007 Regulations No.236 **"Procedure of Granting and Execution of Allocations"**, regulating the procedure of granting allocations to the budget-fund institutions of the Treasury, on the basis of the approved financing plans of a budget-fund institution or its activities, and ensures execution of the allocation;

2) Cabinet of Ministers 3 July 2007 Regulations No.464 **"Procedure of Suspending of the EU Policy Allocations"** , regulating the procedure in which the Treasury temporarily suspends allocation of the implementation of a project belonging to a party receiving support from EU policy instruments , if project implementation reports have not been submitted timely;

3) Cabinet of Ministers 6 November 2007 Instruction No.17 **"Procedure of Payment Execution in the Treasury"** , in order to improve the process of government budget execution and to regulate the procedure of payment execution in the Treasury.

1.2. Accounting and reporting

In 2007, in compliance with Article 32 of the Law on Budget and Financial Management, the Report on the Republic of Latvia's Central Government Budget Execution and Local Government Budgets 2006 was prepared and, after having been approved by the Cabinet of Ministers, together with the Republic of Latvia State Audit Office's **"Opinion concerning the Report on the Republic of Latvia's Central Government Budget Execution and Local Government Budgets 2006"** and "Statement on the Report on the Republic of Latvia's Central Government Budget Execution and Local Government Budgets 2006", was submitted to the Saeima (Parliament) (3 volumes, 779 pages). The report is prepared in compliance with the requirements and structure of Article 31 of the Law on Budget and Financial Management determined in Cabinet of Ministers 5 June 2007 Regulations No.367 "Regulations on the Procedure of Preparing the Accounting Year Report", for the period of 1 January 2006 to 31 December 2006, and **summarizing information from 28 reports submitted by Ministries and Central State Institutions, and from 553 reports submitted by local governments.** Annexes on execution of the central government budget are prepared in compliance with the structure determined by the Law on Government Budget.

In compliance with Cabinet of Ministers 12 December 2006 Regulations No.1008 "Regulations on the National Statistical Information Programme 2007" , programme sections "National Accounts System in compliance with reformed methodology by the European National and Regional Account System in European Community (ESA-95) and United Nations Organization" and "Public finance, banks and other financial institutions and cash circulation", **the Treasury's monthly, quarterly and annual reports on the central government budget execution and local government budgets**, are used as a source of information by the Central Statistical Bureau and the Bank of Latvia, who are responsible for the statistical information to be reported in accordance with the requirements set by the EU legislation. The Treasury is responsible for the statistical information on the execution of the government and local government budget to be prepared in accordance with the programme section "Public finance, banks and other financial institutions and cash circulation" sub-sections "Statistical information to be prepared based on other regular requests of international institutions" and "Statistical information to be regularly prepared based on domestic user requirements".

In accordance with the request of the most significant users (EUROSTAT, ECB, International Financial Institutions, as well as Saeima, the State Audit Office, the Ministry of Finance, the Bank of Latvia, CSB), **additional information on execution of the government and local government budget** during the financial year, accounting quarter and month, as well as **the government and local government statistical financial information** during the accounting month, quarter and financial year, is summarised from their direct sources.

In compliance with the authority delegated by the Law on Budget and Financial Management, in 2007 the Treasury drafted the following laws and **regulations of the Cabinet of Ministers, setting universal accounting principles for the central and local government budget institutions**, creating a legal framework compliant with international standards as well as a procedure for the preparation and submission of reports:

1) 13 November 2007 Cabinet of Ministers Regulations No.763 **"Amendments to Cabinet of Ministers 25 April 2006 Regulations No. 313 'Regulations on the Contents of Monthly Local Government Reports, Their Preparation and Submission Procedure'"**, taking effect on 1 February 2008;

2) 5 June 2007 Cabinet of Ministers Regulations No.367 **"Regulations on Procedure of Preparing of the Report for Accounting Year"**, which took effect on 13 June 2007. In compliance with the fourth part of the Article 31 of the Law on Budget and Finance Management, the Ministry of Finances prepares the Report on

Accounting Year in accordance with the procedure established by the Cabinet of Ministers. In order to ensure involved competent institutions with a unitary and timely understanding of information to be obtained form annual reports, the content and volume of the report, their forms and appendices, the general principles and procedure of preparation are determined for each report. The above-mentioned conditions determine the form of financial and budget execution information to be indicated, as well as what explanations shall be provided for significant changes in the accounting year;

3) 13 November 2007 Cabinet of Ministers Regulations No.749 **"Regulations on Procedure of Preparing of the Report for Accounting Year in State-fund and Local Government Institutions"**, which determines how the first report for 2007 shall be submitted. Classification of the information to be included in the report is determined by other laws and regulations, where some changes are made annually. Thus, it was necessary to determine a flexible form for the Account Year Report so it would be possible to prepare the Accounting Year Report without making changes to the content of the form, and in which information in accordance with the requirements of other laws and regulations may be included;

4) 4 December 2007 Cabinet of Ministers Regulations No. 832 **"Amendments to Regulation No.867 'Accounting Procedure for Budget Institutions' from 15 November 2005"**. The Regulation takes effect on 1 January 2008. Changes were made in compliance with current events in International Accounting Standards in order to improve the quality of the consolidated reviews;

5) 4 December 2007 Cabinet of Ministers Regulations No. 826 **"Amendments to Cabinet of Ministers 21 June 2005 Regulations No. 440 'Regulations on the Depreciation Norms of Fixed Assets for Budget Institutions and conditions of their use'"**, taking effect in 2008. The Regulation has been supplemented by a provision in relation to the accounting of used fixed assets, if transfer or receipt of fixed assets occurs among institutions of the general government sector. The above-mentioned amendment was required in compliance with 15 November 2005 Cabinet of Ministers Regulations No.867 "Procedure of Accounting for Budget Institutions", where a unitary procedure for transfer/receipt of fixed assets is established within the framework of the general government sector.

In preparation of the above laws and regulations, the Treasury held active consultations with accountants-practitioners working in local governments and ministries as to the application of the provisions to be incorporated in the draft Regulations, thus providing information about the expected changes to local governments and ministries well in advance and ensuring information exchange with the Treasury as to the potential problems and their prevention when applying those provisions.

The Treasury provides government budget and local government institutions with consultations on a regular basis regarding report preparation and accounting issues. On its Internet homepage, the Treasury issues information on methods, current events and services to institutions and local governments. In order to ensure provision of high-quality services for local governments, in 2007, the Treasury issued **informative material on services proposed for local governments** on its Internet homepage, including investments, loans, opening and servicing of accounts and electronic settlement system services.

The Treasury maintains **government budget accounting policy**, taking into account changes and amendments to accounting plans, and determines necessary changes to **the current procedure of transaction accounting** in compliance with changes in the classification of income and expenditure, by performing respective corrections in the government accounting system. In order for the government to elaborate, approve and apply a **unitary budget execution and financial management procedure**, changes were made in the Treasury's government budget accounting plan performed during the execution of the budget to implement processes of the Treasury's unitary government budget planning and execution information system in the model of budget execution, and the "Amendments to the Policy of the Treasury's Government Budget Accounting" were elaborated and approved, with the addition of section "Accounting of Investment Securities".

In order to improve the accounting of budget and local government institutions, ensuring compliance of financial reports with the International Public Sector Accounting Standard, basic statements of International Accounting Standards, 4 December 2007 Cabinet of Ministers Regulations No.832 **"Amendments to 15 November 2005 Cabinet of Ministers Regulations No. 867 "Procedure for Accounting for Budget Institutions""**, were approved. **The Regulations are supplemented by the most significant accounting norms, providing a unitary model of stock accounting for budget institutions, accounting of financial instruments, assessment of their accounting principles and supplementing in accordance with changes to International Accounting Standards**, which will improve the quality of financial information. The Regulations are supplemented by the norm, **providing detailed accounting of fixed assets** (recognition, assessment, re-assessment in compliance with the cadastre value, alienation, transfer with no reward among budget institutions) and **separate stock for fixed assets and liabilities**. The laws and regulations determine a **unitary division of fixed assets and liabilities of the budget institution** in accordance with the accounting plan, and

provide explanation on recognition of fixed assets and liabilities in a particular account. Amendments in the account plan have been made to the Regulations, detalisation of particular accounts has been determined and respective accounting explanations have been provided.

1.3. Electronic services development

Implementation of Unitary Government Budget Planning and Execution Information System

In 2007, the work on the joint project started in 2006 with the Ministry of Finance, **"Implementation of Unitary Government Budget Planning and Execution Information System"**, was continued. Through implementing the first stage of the project, the opportunity to perform centralised summary and processing of budget plans was ensured, making this process less time-consuming and more adequate for opportunities provided by information technologies. Within the framework of the project, the technical infrastructure was fully implemented, providing accessibility and safety for the system. In order to ensure effective use of financial and human resources, The Treasury has established a common information technology infrastructure in collaboration with the Ministry of Finance to ensure centralised system management.

Summary system for budget reports

Since 2006, submitters of reports from budget institutions may submit and validate their monthly and quarter reports to the Treasury electronically. **A system for aggregation of annual**, quarter and monthly reports is being used for reports submitted by Ministries, central government and local government institutions, and is based on the latest technological achievements and uses the on-line Internet mode. In order to develop electronic services and on-line information exchange with the clients of the Treasury, and to maintain a unitary government and local government budget report system and system of statistic reports, an assessment of the current programme was performed in 2007 for further development of the report system, system solutions and specifications elaborated, and the best solution and its compliance with the possibilities provided by the budget determined.

Electronic settlement system of the government budget *eKase*

Already for the fourth year, the Treasury has been using ***eKase* (electronic settlement system of the government budget)**, which has been elaborated to provide the Treasury services over the Internet. Via *eKase*, the Treasury grants remote access to services to institutions financed from the budget and local governments, at the same time guaranteeing security and confidentiality of information. Using the *eKase*, the Treasury's clients can:

1) make payments;

2) check the results of implementation of the payment instructions;

3) receive financial information on account position, implementation of the financial plans of the central government budget, statements of account turnover and monthly account summaries.

In 2007, 192 clients signed cooperation agreements to use the *eKase* system and overall 1462 clients with more than 4000 users use *eKase* services. The overall share of the lats flow payments processed through the *eKase* in comparison with the total lats flow was 62%. In comparison with 2006, the volume of payments in 2007 processed via the *eKase* increased by 6%. This expansion was due to the growing number of the users of the service.

In March 2007, after perfecting the system and implementing a safer authentication solution – dynamic password generators – **testing of the safety of the *eKase* system** was performed in collaboration with "Biti" SIA. The purpose of the audit was to acquire additional confidence on the safety of using the system. No significant safety problems with the authentication of users, authorisation of payments and saving of auditing records were encountered. Integration of the dynamic code generator solution into the system was tested within the framework of authentication tests. No significant problems were observed. Consequently, *eKase* system was recognized as safe for use. In 2007, after the invention of the dynamic code generators, authentication tools for the first eKase users with signatory powers were gradually replaced by dynamic code generators. Thus, with the heightened safety level of authentication tools, **safety against unauthorized access to the *eKase* system is improved.**

Credit cards attached to the Treasury's accounts

As of 1 January 2007, the Treasury has implemented compatibility of the information systems in collaboration with "Hansabanka" AS, in order to ensure work with **Credit cards attached to the Treasury's accounts** and to provide budget institutions the opportunity to perform budget expenditures with credit cards. Credit card services are provided for expenditures incurred by staff on business trips and visits, as well as running expenses. When introducing the credit cards linked to the Treasury's accounts, employees of government budget institutions are enabled to make cashless payments during their business trips, complying with the Law on Budget and Finance Management, which requires that government expenditures are made from accounts opened with the Treasury. In 2007, 161 budget institutions concluded agreements on use of the service and 1198 credit cards were issued.

Introduction of payment cards by collecting government budget payments and charge for services provided by the budget institutions

In order to ensure execution of the task provided in the Government Declaration: **to ensure the**

opportunity to use payment cards by collecting government budget payments and charge for services provided by the budget institutions (for instance: dues, penalties, etc.), the Treasury, after gathering information on possible solutions for the use of payments cards, concluded that the common system of accepting payment cards is not adequate for the specific character of the budget settlements – in comparison with the common practice of processing payment cards, it is important for the budget settlement accounting to receive detailed data on the payer.

The Treasury elaborated solution of payment cards appropriate for the specific of settlements and in September 11, 2007, declared open tender on acceptance of *MasterCard* and *VISA* system and payment for transactions performed by these cards. The subject of the Tender involves acceptance of these cards both installation and servicing of POS terminals. This service will be available to population in all the budget institutions providing paid services or collecting charges, penalties and other costs (except tax payments). This service will be provided to the population free of charge. All the commission payments in relation to servicing the cards will be covered from the servicing assets of the government budget. The tender Commission, after assessment of submitted proposals, declared proposal by "SEB Latvijas Unibanka" AS as the most adequate to the Tender Regulation.

Operation in Trans-European Automated Real-time Gross settlement Express Transfer system TARGET2

On 19 November 2007, the Treasury (as a direct participant) **commenced its operation in Trans-European Automated Real-time Gross settlement Express Transfer system TARGET2**, in order to ensure an effective, quick and safe infrastructure for large-volume and urgent payments in euro for clients of the Treasury.

Euro payment system TARGET is a real time payment system used by the Central Banks of the EU Member States within the European Monetary Union and together with the ECB to implement common monetary policy and facilitate the operative performance of the euro payment system. Banks of the EU use the system for financial market settlements as well as payments by their clients.

On 24 October 2002, the Board of the ECB made a strategic decision to change TARGET by replacing it with a technologically new system, TARGET2, which significantly increases the efficiency of payments within Europe and offers the opportunity for further integration of the financial infrastructures in Europe. The principal benefit of the new system – a common technical platform providing equal conditions for all states entered in TARGET2, as well as the opportunity to involve new countries. It is expected that the new system will be one of the most modern and effective payment systems in the world.

In order to execute successful joining or migration of Latvia to the TARGET2 system with the first migration group, which consists of the Central Banks of Austria, Cyprus, Germany, Latvia, Lithuania, Luxembourg, Malta and Slovenia, and respective users of TARGET2, the Treasury has performed all the necessary measures for adopting internal information systems and preparation and signing of necessary legal documents.

Participation in Electronic Clearing system of the Bank of Latvia for settlements in euro

In order to adjust to the Electronic Clearing system of the Bank of Latvia, which will provide processing of small payments in euro, the Treasury gathered information on necessary changes in information systems and elaborated the domestic strategy for the use of the euro Electronic Clearing system. In November and December of 2007, the Treasury successfully participated in euro clearing tests organised by the Bank of Latvia. On 21 December 2007, the Treasury and the Bank of Latvia concluded **an agreement on performance of payments in euro in the clearing system of the Bank of Latvia.**

Starting in 2008, the Treasury will have the opportunity to use the clearing system of the Bank of Latvia, which will provide the opportunity **to perform payments in euro between the Treasury and banks of Latvia within one working day**, without using foreign corresponding banks and in the same way payments are currently made in lats.

1.4. Concept of development of services provided by the Treasury's settlement centres

Keeping in mind that, as of 1 June 2009, the administrative-territorial reform will be performed in the state, the administrative-territorial division will be changed and, taking into account the fact that the main clients of the Treasury's regional centres are local governments and their institutions, in 2007 the Treasury commenced prior investigations on how this process may influence further operations of the Treasury's regional centres and services provided by them. The formed work team assessed functions of the regional centres, issues related to the development of personnel in these settlement centres, observance of information safety requirements, distribution of obligations among employees, role of settlement centres within the framework of the implementation of the Treasury's functions, and compliance of the client service process with the procedure provided in the documents of quality management of the Treasury. In 2008, the Treasury will elaborate possible models of development for the settlement centres, taking into account execution of tasks determined in the Strategy: to increase the number of settlement centres in an *on-line* mode by offering the opportunity to receive modern financial services and setting consultation services for clients as the primary function of settlement centre employees.

2. Central Government debt, cash and budget loan management

In compliance with the authorisation given by the Minister of Finance, **the Treasury performs management of the central government debt and temporarily free central government budget cash, engages in financial derivatives deals and other deals within the framework of the central government debt management as well as organises granting and monitoring of the central government budget loans and guarantees.**

The annual Law on the State Budget sets the **maximum allowable level of outstanding government debt as at the end of the year**, whereas **objectives, basic principles and tasks of the central government debt portfolio and borrowing management within the framework of the medium-term government debt management are established by the Latvian Central Government Debt Management Strategy** approved by the Minister of Finance.

In compliance with the Latvian Central Government Debt Management Strategy, **government debt portfolio management** is careful and oriented to limitation and prevention of financial risks, allowing use of derivatives, determined in the Latvian Central Government Debt Management Strategy, only to ensure management of finance risks. The approach of government loan management is loan opportunity oriented to ensure liquidity and beneficial loan conditions.

The amount of government borrowing, central government debt and the respective costs to be set aside to meet the debt commitments are affected by **the size of the overall financing need**, comprised of the fiscal deficit to be financed from the central government budget, the amount of central government debt commitments to be settled, as well as the amount of the required reserve liquidity to ensure the implementation of the central government budget cycle and commitments. Planned measures to satisfy the overall financing need within the current year and the financial instruments best suited for financing are prescribed in **an annual Medium-Term Funding Plan**, which is developed by the Treasury, based on the guidelines established in the Latvian Central Government Debt Management Strategy and approved by the Minister of Finance. Prior to approval, the opinion of the Bank of Latvia is sought.

The Treasury Cash Management Strategy approved by the Minister of Finance establishes the goals, tasks, basic principles and responsibility of the Treasury by performing timely and effective **cash management**, observing liquidity requirements and restricting financial risks. Within the framework of **temporarily free fund management**, the Treasury organises **financial resource placement** for collaboration with both local and foreign business partners. In order to ensure a more effective management of government budgetary assets, the Treasury has invested in fixed income loan securities, in addition to placing resources in time deposits. To more effectively manage financial risks related to these transactions, the transactions are made with regard to cooperative limits, which are established for each of the Treasury's business partners depending on the type of the financial instrument in question. **A financial risk management framework** is developed to supplement the management of fixed income loan security profiles; it includes several internationally practiced and accepted security profile management instruments and tactics.

Within the framework of the central government debt management, the Treasury organises the visits of analysts from the three largest **international rating agencies** (*Fitch Ratings, Standard & Poor`s* and *Moody`s Investors Service*) to Latvia, thus providing investors with an opportunity to receive the latest information about Latvia, and analyse the opinion concerning Latvia's development trends and potential risks. Investors use this information to assess investment opportunities in Latvia (including investment into government-issued securities). Therefore, a **credit rating** is an important factor for Latvia ensuring availability of financing, which affects the price of borrowing. Rating agencies upgrade the credit rating of the Republic of Latvia and review its future outlook on an annual basis and also grant ratings to each specific government-issued security. Currently, **Latvia credit rating for long-term liabilities in foreign currency** is **A2** (*Moody`s Investors Service*)/**BBB+** (*Standard& Poor's* and *Fitch Ratings*) with **stable** (*Moody`s Investors Service*)/**negative** (*Standard&Poor's* and *Fitch Ratings*) **future assessment (*outlook*).**

The Treasury participates in the process of **guarantees issue on behalf of the government** by examining and evaluating the risks pertaining to granting government guarantees. The Treasury organises the process, in order to ensure signing of the guarantee agreements: i.e., participates in drafting of the guarantee agreements, guarantee service and guarantee collateral agreements. After the guarantee agreements have been signed, the Treasury keeps accounts of the commitments associated with guarantees issued on behalf of the government. The maximum size of guarantees issued on behalf of the government and project implementers are set in the annual law on State budget.

2.1. Central Government Debt Management Strategy

In 2007, the Treasury fully implemented the **Latvian Central Government Debt Management Strategy** approved by the Minister of Finance. Borrowing was made in line with the basic principles established in the Latvian Central Government Debt Management Strategy, and financial derivatives were applied, in order to ensure compliance with the debt portfolio parameters prescribed by the Latvian Central Government Debt Management Strategy.

The Latvian Central Government Debt Management Strategy **sets the central government debt management goals and objectives**. The Latvian Central Government Debt Management Strategy outlines the **medium-term** operations of the Treasury in managing the central government debt in line with the economic development trends as well as the situation on Latvian and global financial markets.

Latvian Central Government Debt Management Strategy distinguishes between debt portfolio management and borrowing management. The goal of the **central government debt portfolio management is to manage the financial risks of the central government debt portfolio.** Thus, several **parameters of the central government debt portfolio structure** have been set for the purpose of achieving this objective:

1) the share of the lats debt;

2) maturity profile;

3) the share of the fixed rate;

4) interest rate duration;

5) currency composition for the net foreign currency debt.

The goal of the central government borrowing management is to ensure the availability of the necessary financial resources and their liquidity for financing the deficit of the central government budget and refinancing of the central government debt as well as borrowing on favourable terms and conditions. Several basic principles were established for the purpose of achieving this objective:

1) to ensure continuous opportunities for attracting financial resources;

2) to maintain the daily minimum reserve liquidity;

3) to perform each borrowing transaction in a professional manner;

4) to foster the development of financial markets;

5) when engaging in borrowing transactions, ensure compliance with the basic principles of the central government debt portfolio management;

6) to create an excellent "borrower" image for Latvia.

On 8 August 2007, The Minister of Finance approved the specified Latvian Central Government Debt Management Strategy, where some changes on minimum allowable share of lats within the government budget portfolio were made, taking into account tendencies of development of the **Latvian government capital market and all the financial systems in 2007: decrease of the domestic financial market liquidity and, as a result, significant increase in rate of domestic loan securities.**

Continuing the implementation of the debt portfolio analysis models, the ***Cost-at-risk* model** was improved at the highest level. Its practical application enabled a detailed analysis of the established borrowing scenarios and their potential impact on the debt portfolio parameters. The latest application of the model developed **enables more accurate forecasting of the medium-term central government debt servicing payments.** At the beginning of 2007, the relatively simple *Cost-at-risk* model was used by the Treasury to evaluate the structural parameters of the Latvian central government debt portfolio, and concluded that it is not necessary to change the parameters prescribed in the Latvian Central Government Debt Management Strategy, as they have been set at an optimum level. Yet after the Treasury specialists improved the methodology of the model and software, the model was used within the framework of borrowing scenario simulations for the 2007–2009 Funding Plan, providing additional information required to make a decision as to which of them is the most adequate. Improvements for the *Cost-at-risk* model are planned in 2008, as is the introduction of multiple factor analysis opportunities.

In 2006, the Treasury started to regularly analyse the activity with which **funds are obtained** every month and prepare a detailed assessment of the factors impacting borrowing both within the context of the Latvian and international finance and capital markets. During 2007, the standard effectiveness of loan payments continued to be analysed quarterly and was compared to the loan transaction time and cost benchmarks of 2005. At the end of 2007, proposals were developed for the implementation of the benchmark model methodology.

In 2007, the Treasury prepared an analytical **Central Government Debt Management Report** for 2006, so as to provide the Treasury's clients, including the existing and potential cooperation partners of the Treasury and investors in government securities, with information on the latest developments in the government debt management, performance indicators and future trends. The Central Government Debt Management Report was also sent to other bodies implementing similar government debt management functions in the EU (debt management bureaus). The cooperation partners (including banks) expressed their appreciation of such a form of presenting information on the latest developments in the Latvian central government debt management.

2.2. Changes in the central government debt in 2007

In 2007, the amount of borrowing was initially planned in accordance with the assessment of financing demand, which provided a gradual decrease of the central government budget deficit from the amount set by the Central Government Budget Law for 2007 from 1.4% of the GDP to 0.9% of the GDP in 2009.

However, taking into account increasing macroeconomic risks, in March of 2007, the Cabinet of Ministers supported measures to be taken to limit inflation and to reduce macroeconomic instability, where one of the most significant measures for limiting inflation was the requirement to implement strict fiscal policy within the conditions of sharp economic growth, creating a harmonized and favourable government budget structure for the development of the national economy. Objectives of preparing the government budget including an inflation reduction plan were observed; the previously planned **financial deficit of 177.8 million lats** was changed to a **financial excess of 54.5 million lats.**

In compliance with operative data, **financial excess of central government budget** in 2007 achieved an amount of **117.2 million lats**, significantly exceeding the amount of excess approved in the Amendments to the Central Government Budget Law of 2007.

Consequently, the amount of borrowing necessary for budget lending and refinancing of central government debt, as well as for ensuring reserves of liquid cash in 2007, was less than was previously planned.

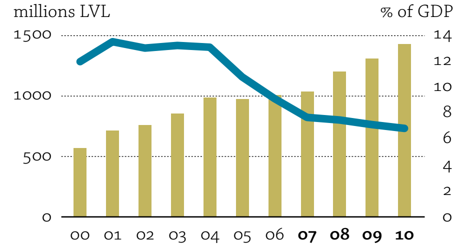
In 2007, short-term government domestic borowing bond emissions with a maturity profile of six and twelve months, mid-term bonds with a maturity profiles of two, and five year extensions and a long-term bond emission programme with a maturity profile of 11 years, were used from the government's domestic borrowing instruments to cover financial necessities.

The amount of resources acquired from securities public auctions in 2007 in the domestic financial market was **95.3 million lats.** In November of 2007, in order to ensure the liquidity, a **short-term loan** from domestic credit institutions of **18.5 million euro (13 million lats)** was taken.

The amount of borrowing made in foreign financial markets in 2007 from international financial institutions was **70.4 million lats.** The largest of these were the 75 million euro (52.7 million lats) EIB loan for co-financing EU Structural Funds and Cohesion Fund projects, and the loan of 25 million euro (17.6 million lats) provided by foreign commercial banks. Taking into account borrowing and settlement of the debt, **central government debt** in 2007 has increased by 30.7 million lats and, in accordance with the operative data on 31 December 2007, was **1 031.8 million lats** in nominal value or 7.4% of the GDP, without exceeding the allowed maximum debt of 1 335.0 million lats in by the end of the year, as stated in the amendment to the law "On the Government Budget 2007".

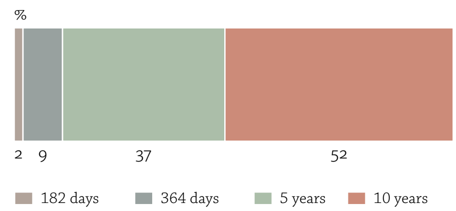
Taking into account forecasts by the Treasury and the Ministry of Finance, the government debt in the middle-term period will not exceed 10% of the GDP (see Chart 1).

Chart 1. **Central government debt (nominal value) in 2000-2010**



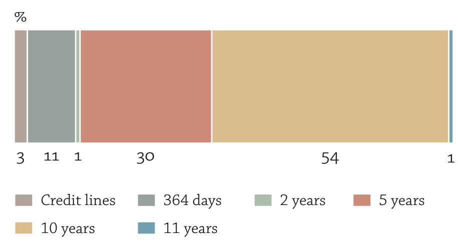
Source: the Treasury

Chart 2. **Domestic central government debt on 31 December 2006**



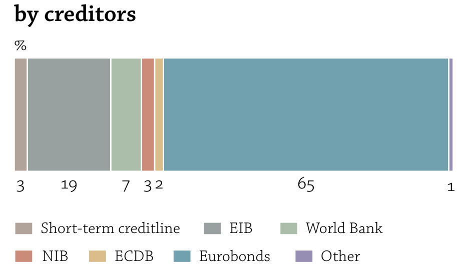
Source: the Treasury

Chart 3. **Domestic central government debt on 31 December 2007**



Source: the Treasury

Chart 4. **Foreign debt of the government on 31 December 2007 by creditors**



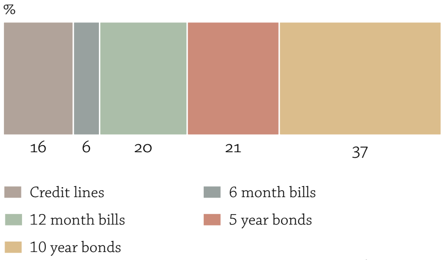
Source: the Treasury

Table 2. **Domestic government borrowing securities in 2007**

Type of securities	2006 (million LVL)	2007 (million LVL)	Difference (+/-) million LVL
6 month bills	12,86	16,46	+3,6
12 month bills	39,709	45,309	+5,6
2 year bonds	–	2,218	+2,218
5 year bonds	42,275	31,41	-10,865
10 year bonds	72,031	–	-72,031
12 year bonds	–	2,120	+2,120
Total	**166,875**	**97,517**	**-69,358**

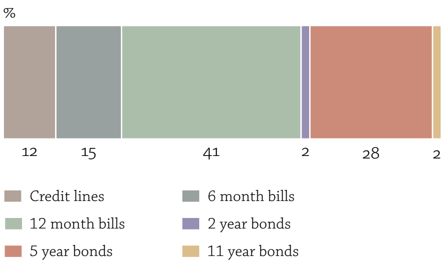
Source: The Treasury

Chart 5. **Domestic loans performed in 2006**



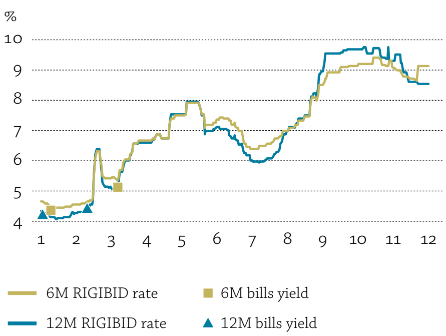
Source: the Treasury

Chart 6. **Domestic loans performed in 2007**



Source: the Treasury

Chart 7. **Yields of six and twelve month bills and six and twelve month RIGIBID rates in 2007**



Source: the Treasury

2.3. Central government domestic debt

On 31 December 2007, the **central government domestic debt (in lats)** amounted to **396.743 million lats** at nominal, of which 96.72% was comprised of domestic securities and 3.27% of credit lines (as well as borrowing of budget institutions outside the Treasury – 0.01%). In 2007, **a decrease in domestic (lats) debt by 21.97 million lats** was observed.

2.4. Central government foreign debt

On 31 December 2007, **the central government foreign debt (foreign currency) amounted to 635.091 million lats.**

In 2007, the **foreign debt of the central government increased by 53.62 million lats.** The expansion of the foreign debt is due to the fact that available financing from EIB was used for ensuring government co-financing of EU structural funds and Cohesion Fund projects, performing the second loan disbursement amounting to 75 million euro. On 31 December 2007, the **major part** (65%) of the **central government foreign debt** consisted of borrowing on the capital market, i.e. **euro bonds maturing in 2008 and 2014.**

2.5. Management of the central government borrowing

Domestic borrowings

In 2007, the share of current domestic securities in the domestic debt saw a slight change.

In 2007, the amount of **domestic market securities** issued was considerably lower than the planned amount (**97.52 million lats** in total). The amount issued was reduced mainly on account of better performance of the central government budget and the sharp increase of the rate of lats paired with the inconsistent demand of domestic market securities. In 2007, the **amount of government securities declined** by **35.37 million lats** to hold at 383.3 million lats. In contrast to the previous year, mostly short-term resources (6- and 12-month bills) as well as bank credit lines were used for financing, amounting to 68% of the total financing, whereas long-term resources accounted for 42% of the total financing.

Due to lack of liquidity of lats on the interbank market, **activity of investors in sales of central government domestic loan securities** in 2007 was very low. The average level of yields of lats in bond auctions **achieved record levels.**

In order to make payments in the most favourable conditions, a decision was made to organise several terms of security sales, ensuring participants of the market opportunity to choose the most suitable investment term.

Despite the fact that the amounts offered at competing sales in the last year were comparatively small, the demand of auctions in 2007 was often smaller. Because the rates of competing sales offered to participants (especially in the second half of the year) exceeded the Treasury's ideal level of allocated resources, securities were not sold during several consecutive sales (fixed sale amounts were not organised).

Table 3. **Compliance of the Central Government Debt Composition Parameters with the Central Government Debt Portfolio Composition Parameters established by the Latvian Central Government Debt Management Strategy**

Parameters	on 31.12.2006.		on 31.12.2007.		Strategy	
Share of the lats debt, %	42		37		> 25[3]	
Maturity profile, %	< 1 year 13	< 3 years 30	< 1 year 22	< 3 years 30	< 1 year < 25	< 3 years < 50
Share of fixed rates, %	64,65		60,18		60 - 70	
Interest rate duration (in years)	3,07		3,38		3,25 (+/- 0,25)	
Currency composition of net foreign currency debt, %	EUR 98,92		EUR 99,82		EUR 100 (+/-) 5	

Source: The Treasury

[3] If within one half of the year middle-term and long-term loans by the Treasury increase in price and government domestic loan securities rate on the securities market is less than 100 basic points over EUR standard rates (within the respective term EUR SWAP), the minimal share of debt in lats shall be ensured at least at level of 35% no later than within one year.

Foreign borrowing

In 2007, the Treasury used available **financing from the EIB** for the loan of EU Structural funds and Cohesion funds project to granting government co-financing of **75 million euro.**

In 2007, a **decision on the issue of Eurobonds of 500 million euro** was made. Due to the high level of uncertainty in the international finance markets, resulting from problems in mortgage credits in the U.S.A. (*subprime*), which caused a lack of liquidity and increase of credit risks in financial markets, **the issue of Latvian euro bonds was postponed to 2008.**

2.6. Central government debt portfolio management

In order to assess how the Latvian Central Government Debt Management Strategy has been implemented, the actual debt portfolio composition parameters on 31 December 2007 have been compared against the debt portfolio composition parameters on 31 December 2006 and the debt portfolio composition parameters set in the Strategy.

In order to expand the range of financial instruments to be used within the framework of management of central government debt and cash assets, the Treasury has commenced implementation of optional transaction opportunities: in 2007, an assessment model project was elaborated, which incorporates calculators for various types of financial options, by which one may perform estimation of option premium, using various methods for determining price volatility.

2.7. Central government loans

The process of issuing government loans is **controlled by the Law on Budget and Financial Management**, the annual law on government budget, and Cabinet of Ministers 19 June 2007 Regulations No.395 **"Procedures for the Issue and Servicing of State Loans"**.

In 2007, amendments were made to the Law on Budget and Financial Management by **determining for what purposes government loans may be issued**, i.e. for budget and financial management, for financial stabilization, to implement student crediting programmes, to implement investment project and commercial support programmes, to implement projects and events co-financed by the EU, as well as to implement projects funded by foreign programmes. The law determines **the circle of receivers of the loans**: local governments, executors of government special budget and student crediting programmes, institutions financed from budget, capital corporations, unions and foundations.

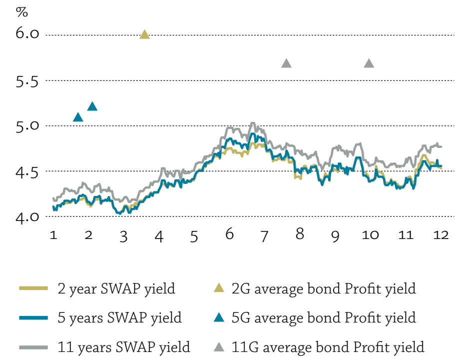
Government loans are being issued every year in amounts determined by the annual government budget law. In 2007, loans amounting to 124 177 008 lats were granted from the government budget. Tendency of previous years has been preserved during the year of account, and **the majority of government loans has been received by local governments** (**96%** of total amount of loans granted) for the implementation of autonomous functions, projects and events co-funded by the EU, as well as for other purposes.

On 31 December **2007**, **the local government debt to the Treasury** amounted to **250 million lats**, representing **an increase of 83 million lats** in comparison with 31 December 2006.

On 19 June 2007, a new procedure for determining government loan interest rates was included in Regulations No.395 **"Procedure for the Issue of State Loans to Local Governments and Changes in the Conditions of Loans"**, which ensures **the Treasury may offer loan conditions more flexible and adequate for the economic situation.** It can be attested to by the fact that, in 2007, local governments received direct loans from the Treasury amounting to 88% (in 2006 – 82%) of the total loans received during the year of account (both from the Treasury and another creditor). **A local government may receive loans from other creditors only with the consent of the Minister of Finance and if loan conditions offered by the other creditor are more favourable than those of the Treasury.**

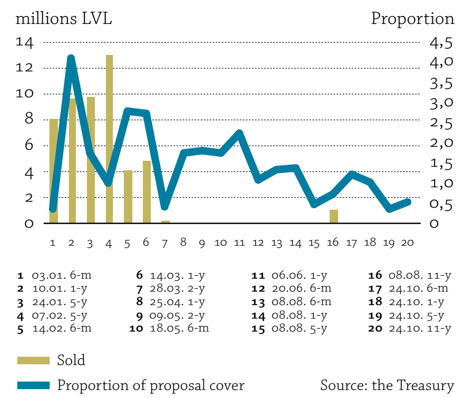
Taking into account predominant tendencies in financial markets, at the end of 2007, decision **to reduce the amount of charges to local**

Chart 8. **Two, five and eleven year bond yields and two, five and 11-year Euro SWAP rates in 2007**



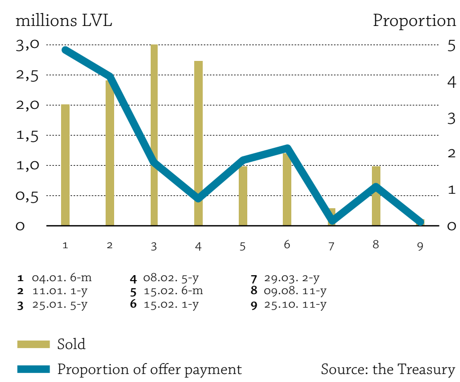
Source: the Treasury

Chart 9. **Primary trade activity of the government securities in competing multi-price auctions in 2007**



Source: the Treasury

Chart 10. **Primary trade activity of the government securities in fixed rate auctions in 2007**



Source: the Treasury

Chart 11. **Loans to local governments from 2003 to 2007**

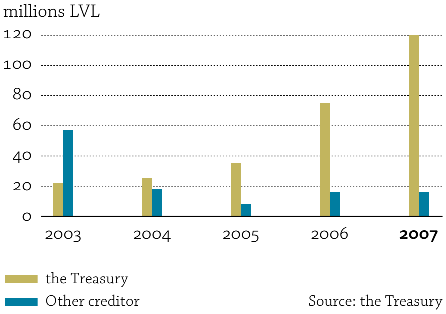


Chart 12. **Guarantees issued by the State from 2001 to 2007**

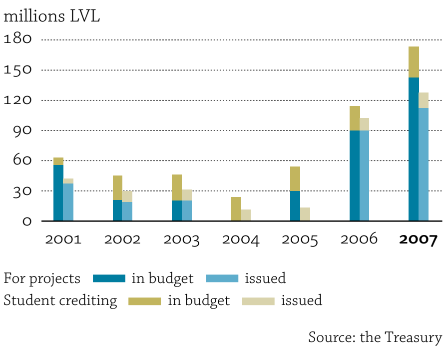


Chart 13. **Outstanding amounts of government guaranteed loans in 2007**

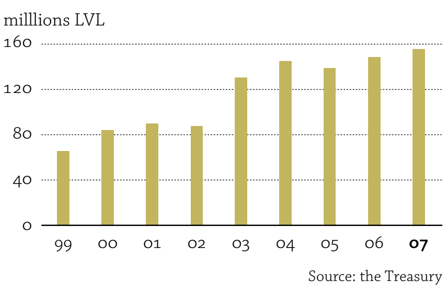
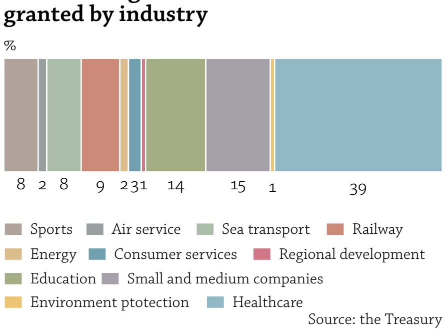


Chart 14. **State guaranteed loans granted by industry**



governments for issuing and servicing government loans – from 0.5% to 0.25% per year – of the amount of the loan itself, thus allowing local governments to reduce expenditures for servicing the loans and transfer available assets to other autonomous functions, including solving social issues. Furthermore, **the fee for issuing and servicing government loans for executors of special budgets and the sub-programme "Crediting of students and studies" was cancelled.**

2.8. State guarantees

Article 37 of the Law on Budget and Financial Management stipulates that only the Minister of Finance has the authority to grant guarantees in the name of the State within the limits set in the annual law on State budget, committing public funds to implement the Public Investment Programme projects and business support programmes as well as study and student credits. Guarantees are issued in accordance with the Cabinet of Ministers 12 July 2005 Regulations No.513 **"Procedure for Issuing and Monitoring Guarantees".**

Within the Law on Government Budget 2007, guarantees were allocated in the amounts of 1.72 million lats to "Vidusdaugavas SPAAO" SIA and 0.97 million lats to "Alba-5" SIA for the implementation of the co-financed EU Cohesion Fund waste management project, and 7.40 million lats total for the Latvian Olympic Committee's construction and reconstruction projects of the sports arenas in Jelgava and Ventspils, a loan recrediting guarantee for the management of the Roja port in the amount of 0.51 million lats, crediting for students and studies in the amount of 29.70 million lats, as well as 103.97 million lats total for three reconstruction projects in Latvian hospitals and 1.90 million lats for the reconstruction and facility installation of Riga's Stradina University lecture halls. **All guarantees granted were in the planned amount**, with the exception of the guarantees for "Alba-5" SIA, which requested only 0.47 of the 0.97 million lats planned, and the student and studies crediting guarantees of 14.85 million lats.

At the end of 2007, **the remainder of loans guaranteed by the State** increased in comparison to 2006 and was **158.11 million lats** (see Chart 13).

State guaranteed loans have been granted for the support of various industries (Chart 14). **During the recent years, support for healthcare institutions has increased**, and as such, the amount of guarantees issued for healthcare institutions is the highest.

The major part of loans guaranteed by the State is received **from foreign creditors – 74%.** The remaining 26% are issued by local credit institutions. The largest creditor for state guaranteed loans is DEPFA plc Bank, which has issued 33% of the total amount; it is followed by the EIB – 23.9% and ZIB – 13.5% of the total amount. The largest amount of loans from local creditors comes from Parex Bank – 4.8% of the total amount.

In 2008, State guarantees for the planned total amount of 45.1 million lats will be provided, of which 23.8 million lats are allocated for crediting studies and students and 14.5 million lats to support three projects of the Latvian Olympic Committee.

2.9. Liquidity management

The **objective** of liquidity management is **to ensure availability of cash to meet the financial commitments** in due time and in the full amount. The Treasury sets the requirements **for providing cash liquidity** and **a procedure for meeting the liquidity requirements.**

The Treasury engages in the following activities with a view to comply with the liquidity providing requirements:

1) monitors the stock of liquid cash as well as compliance with the liquidity limits and size of the liquid cash reserve;

2) timely identifies and prevents situations that may impair the cash liquidity and result in a payment or liquidity crisis;

3) ensures constant opportunities to borrow cash by concluding respective agreements with domestic and international

financial market participants (credit institutions);

4) places the temporarily free funds, so as to maintain an adequate stock of liquidity that would ensure the required liquid cash reserve and compliance with liquidity limits within the relevant period.

In its daily cash management, the Treasury complies with the set liquidity provision requirements, thus mitigating the probability of a risk of payment or liquidity crisis materialising.

In 2007, the Treasury ensured the availability of the **required liquid cash every day**, based on the financing needs and financial market developments, as well as placed the temporarily free funds, maintaining **the necessary liquid financial resource reserves** and complying with **the liquidity limits**. It also monitored **the stock of liquid cash** - it complied with the liquidity limits and maintenance of the liquid cash reserve. In 2007, available cash balances were used to provide liquidity. The balances had increased as a result of government budget surplus (the governments short-term domestic loan bonds and maturity profiles of six and twelve months, as well as mid-term bonds with a maturity profile with two and five year extensions and long-term bond emission programmes with a maturity profile of 11 years). Funds were also raised on both the domestic financial market and foreign financial market (a loan from EIB to ensure the co-financing of projects financed by the EU Cohesion and Structural Funds, as well as short-term loans from foreign banks). When necessary, additional liquidity was raised by resorting to the established standby borrowing facility.

In order to **implement the Cash management strategy**, in 2007, the Treasury commenced the introduction of the **investment market value risk assessment model *Value-at-Risk***, which allows to determine possible losses from a particular portfolio of securities and, consequently, may serve as the basis for a decision to purchase a particular security at a particular moment.

In order to improve finance risk management, **an index (*Delta*) of the allowed deviation anticipated in the value of derived financial instruments was introduced** within the framework of the Latvian Government Debt Management Strategy and Cash Management Strategy. The *Delta* index indicates the sensitivity of the respective derived financial instrument against the instability of the basic financial instrument. The *Delta* index indicatively specifies how much the theoretical price of derived financial instruments used changes, as well as how the price of a portfolio changes when the costs of assets, currency or goods change. Introduction of the *Delta* index will allow analysis of possible fluctuations of the derived financial instruments and, in respective cases, limiting the closing of such instruments.

The Treasury observes the principle of prudence within the framework of cash management, limiting partnership party risk. **The Treasury deposits the free financial resources pro tem in the Bank of Latvia, as well as in credit institutions in Latvia and abroad.** Observance of the principle of prudence is being ensured by **defining clear basic principles to determine limits for the Treasury's business partners**, which are based on ratings allocated by international rating agencies, and by individually assessing the development of financial operations of the business partners.

In 2007, new tendencies in the Real Estate market sector were observed due to a decrease in activity, the number of real property operations and market prices. In 2007, new administrative obstacles were invented in order to limit the volume increase in speed crediting. Taking into account the above-mentioned changes, the Treasury, recognizing possible impact of the real property market development tendencies on the stability of bank operations, has begun to summarize and examine available information on the relation of its business partners (commercial banks of Latvia) to the real property market.

In 2007, the Treasury ensured the liquidity in due time and in the required amount, complying with the set liquidity requirements, and at the same time placed the temporarily free funds in compliance with the desirable average benchmark.

2.10. Facilitating public-private partnership

The Treasury has provisionally defined its **potential role in the mechanism of preparing, assessing, financing, implementing and supervising PPP projects**, which is directed to providing financial management function for PPP projects implemented by state and local government.

Although there is a general opinion that no budget assets are required to implement a PPP project, and that implementing such projects does not influence the level of government debt and deficit, as assets from the private sector are being attracted, the Treasury has tried to attract the attention of representatives form the private and public sectors to the fact that the influence of PPP projects on the budget deficit and debt is not unequivocal.

In order to avoid a situation where, when concluding PPP project agreements the government or local government undertakes unjustified long-term obligations and obtains undesirable influence on debt indices, a mechanism is required with which the potential influence of the project on the deficit of the budget and debt can be assessed. The Treasury has performed more in-depth analysis of this issue, including EUROSTAT methodology for assessment of the PPP project's influence. Conclusions of such studies have been presented within the framework of meetings in relation to the PPP project. In 2007, the Treasury participated both on the PPP Consulting Board and in the work team formed by the Ministry of Economics, which must prepare the report on the influence of the PPP project on the government budget and debt. In 2007, the Treasury submitted its proposals for elaboration of the draft law in relation to the PPP project.

3. Implementation of the functions of the Paying and Certifying Authority for the European Union policy instruments

3.1. Function of the Paying Authority

In accordance with the provisions of the EU Regulations, a **Paying Authority** is **one or several national, regional or local institutions or bodies, chosen by the Member State to certify the incurred expenditure, submit payment claims and Declarations of Expenditure, and receive payments from the European Commission.** The Paying Authority, the same as other institutions involved in implementation of the EU policy instruments, must ensure operation of the instruments in compliance with the European Community interests, effective management and monitoring of structural funds in accordance with the provisions of the EU Regulations and guidelines.

The functions of the Paying Authority are to receive the funds from the European Commission and to perform payments to the receivers of the support by the foundations within the shortest term and in full amount.

The Treasury started implementing the Paying Authority functions as of 1 May 2004.

The Treasury has the **functions of the Paying Authority** for the following EU policy instruments:

1) **EU structural funds** – European Regional Development Fund, European Social Fund, European Agricultural Guidance and Guarantee Fund and Financial Instrument for Fisheries Guidance;

2) **Cohesion Fund;**

3) **European Community initiative EQUAL.**

Table 4. **Declarations of expenditure for the EU structural funds submitted to the European Commission and funding received from the European Commission in 2007**

Fund	Claim date	Claimed amount per current Declaration, in thousands of EUR	Amount calculated by the Treasury[4], in thousands of EUR	Amount received from the EU, in thousands of EUR
ERAF	Claimed in 2006		33 493	33 493
ERAF	29.05.2007	7 080	7 080	7 080
ERAF	11.07.2007	17 345	17 345	17 345
ERAF	19.09.2007	15 546	15 546	15 546
ERAF	31.10.2007	31 290	31 290	31 290
ERAF	30.11.2007	47 856	47 856	47 856
Total ERAF		**119 117**	**152 610**	**152 610**
ELVGF	12.02.2007	7 050	7 032	7 032
ELVGF	27.04.2007	9 441	9 342	9 342
ELVGF	11.09.2007	3 093	3 093	3 093
ELVGF	27.12.2007	0	0	0
Total ELVGF		**19 584**	**19 467**	**19 467**
ZVFI	Claimed in 2006		1 764	1 764
ZVFI	05.04.2007	4 877	4 797	4 797
ZVFI	22.08.2007	1 694	1 531	1 531
ZVFI	03.12.2007	990	-	-
Total ZVFI		**7 561**	**8 092**	**8 092**
ESF	Claimed in 2006		21 533	21 533
ESF	10.05.2007	10 201	-	-
ESF	07.08.2007	15 707	-	-
ESF	02.10.2007	12 027	37 821	37 821
ESF	21.11.2007	13 978	22 032	13 978[5]
Total ESF		**51 913**	**81 386**	**73 332**
total		**198 175**	**261 555**	**253 501**

Source: the Treasury

[4] The Treasury calculates the amount to be expected from the European Commission, as the intensity of the European Community financing activities is different throughout a measure and the European Commisison makes reimbursements based on the European Commission financing rate set for the measure in the financial table of the Single Programming Document.

[5] The European Commission withdrew administrative expenditures performed within the framework of the Project amounting to 8 055 thousand euro, on the basis of conclusion by the EC auditors on possible non-related expenditures. The leading institution performs the necessary measures in order to clarify the issue and solve possible problems.

When certifying the expenditure included in the EU policy instrument claims and Declarations of Expenditure, the **task of the Paying Authority is to ascertain the correctness, eligibility of expenditure incurred within the framework of projects and their compliance with the EU Regulations, as well as the sufficiency of the management control systems or checks established by the Intermediate Bodies/ Managing Authority.** In order to ensure the above, the Paying Authority **has the right** to request the **Managing Authority to implement additional controls in the Intermediate Bodies/ Managing Authority, as well as conduct financial controls and audits of the Intermediate Bodies/ Managing Authority.**

In 2007, the Treasury checked **3 536 payment orders** within the **framework of the EU structural funds** and made structural funds disbursements in the amount of **135 559 thousand lats**. **The number of payment orders checked increased by 44%** in comparison to the previous year.

16 EU structural funds Declarations of Expenditure claiming 198 174 thousand euro from the European Commission were submitted to the European Commission in 2007 (see Table 4).

The amounts received from the European Commission coincide with the Treasury's estimates (except the 8 054 545 euro withheld by the European Commission), in compliance with the performance indicators set in the Operational Strategy of the Treasury.

In order to ensure execution of the task defined by the Strategy: "Time of processing of the payments' applications for Structural funds no longer than 20 working days (days) determined by the normative documents" and "Assessment time for verification of the Declaration of Expenditures no longer than that determined by the normative documents (in days)" already initially elaborating internal documents of the Treasury controlling Quality System, and in order to promote use of EU funds, the Treasury as a payment institution has provided **shorter terms of assessment of inquiry for the Declaration of Expenditures and Payments of Structural funds than it is determined by laws and regulations.** Wherewith, during the consideration of the informative report by the Minister for Special Assignments for Administration of EU funds "Informative Report on middle-term measures for ensuring of effective use of the EU structural funds in 2008" at the meeting of the Cabinet of Ministers on September 18, 2007, where several measures have been mentioned, which shall be performed by institutions involved in management of EU Structural funds, in order to ensure use of funds in 2008, the Treasury was not required to specify the terms.

Within the **framework of the Cohesion Fund**, **90 Declarations of Expenditure** were submitted to the European Commission in 2007, of which **six were the final Declarations of Expenditure**, **claiming 115 753 thousand euro** from the European Commission. The Treasury **disbursed 129 901 thousand euro or 91 295 thousand lats** from the Cohesion Fund in 2007.

In 2007, the Treasury **checked 60 payment orders** within the framework of the European Community initiative **EQUAL** and made disbursements from the initiative funds in the amount of **2 396 thousand lats**. In comparison to the previous year, **the number of payment orders checked increased by 15%.**

Within the framework of the European Community initiative EQUAL, **four European Community initiative Declarations of EQUAL Expenditures were submitted** to the European Commission in 2007, **claiming 3 582 thousand euro** from the European Commission (see Table 5).

The fact that the total amount of the sum required for European Agricultural Guidance and Guarantee Fund, the financing instrument of the Fisheries Management and the initiative of the European Community EQAL (as pre-payments and payments of the transitional period) has achieved 95% of the Fund's funding allotment, therefore, in compliance with the provision of the Paragraph 3, Article 32 of the Regulation No. 1290/1999 by the Council of Europe no assets will be enquired until sending of the Final Declaration within the framework of the Fund.

In comparison with the previous year, EU structural funds and European Community initiative Declarations of EQUAL Expenditures Declarations submitted to the European Commission have not increased; however, the **amount of referable expenditures declared for the European Commission and the amount of claim has grown significantly, which indicates that the implementation of the project is successful.** Until 31 December 2007, EQUAL N+2 financing

Table 5. **Declarations of expenditure for the EU initiative EQUAL submitted to the European Commission and funding received from the European Commission in 2007**

Fund	Claim date	Claimed amount per current Declaration, in thousands of EUR	Amount calculated by the Treasury, in thousands of EUR	Amount received from the EU, in thousands of EUR
EQUAL	Claimed in 2006		910	910
EQUAL	20.02.2007	1 254	1 254	1 254
EQUAL	23.05.2007	686	686	686
EQUAL	14.08.2007	1 014	1 014	1 014
EQUAL	26.10.2007	628	628	628
Total EQUAL		**3 582**	**4 492**	**4 492**

Source: the Treasury

Table 6. **Comparison of expenditures certified for the European Commission in 2007 with 2006**

EU policy instrument	2006		2007	
	Sent declarations	Declared expenditures, thous. EUR	Sent declarations	Declared expenditures, thous. EUR
Cohesion fund	55	128 316	90	172 911
Structural funds	15	177 864	16	283 406
EQUAL	4	3 165	4	5 261
Total	**76**	**309 345**	**110**	**461 578**

Source: the Treasury

allocation principle[6] of EU structural funds for 2005 and the European Community initiativewas fulfilled, i.e., payment claims and Declarations of Expenditure were sent, declaring the entire amount of the EU structural funds financing granted in 2005 and the entire amount of the European Community initiative EQUAL financing allocation (committed amount).

The increase in the amount of expenditure declared in 2007 and the number of Cohesion Fund Declarations of Expenditure sent to the European Commission in comparison to 2006 may be observed in Table 6 and suggests that progress in spending has been achieved.

The Treasury is also the Payment Authority for the **financial instruments of the European Economy Area and for the bilateral financial instrument of the Norwegian government.**

On 18 October 2007, the Saeima adopted the **Law on European Economy Area financial instrument and bilateral financial instrument of the Norwegian government.** In compliance with the above-mentioned law, the range of Regulations by the Cabinet of Ministers shall be updated and elaborated. At the end of 2007, Regulations by the Cabinet of Ministers were updated, and the Treasury took an active part in this process as the institution involved within the administration of financial instruments.

In 2007, the **first granting agreements**, as well as several collaboration agreements on administration of financial instruments, were concluded. On the basis of the agreement concluded, donor countries in July, 2007, performed first pre-term payments. In October, 2007, the Treasury as the Payment Authority verified, approved and submitted to the donor countries requests of assets for the financial instruments, for which the donor countries have performed payments already in November. (see Table 7).

3.2. Function of the Certification Authority during the planning period from 2007 to 2013

In compliance with the Law of the EU Structural Funds and Cohesion Fund management, the Treasury will act as a **Certifying Authority** and Paying Authority for the European Regional Development Fund, European Social Fund and Cohesion Fund in the planning period from 2007–2013. The **functions of the Certifying Authority** include **preparation of certified Declarations of Expenditure and payment claims and their submission to the European Commission, as well as certifying that the declared expenditure is compliant with the existing European Community and Member State Regulations.**

In order to establish universal principles for planning, financial management of the EU funding granted for the programming period from 2007–2013 and making disbursements and submitting Declarations, in collaboration with the Ministry of Finance, the Treasury elaborated the Cabinet of Ministers 26 June 2007 Regulations No. 418 **"Procedure of granting government budget assets for implementation of co-financing projects of EU funds as well as procedure of performing the payment and preparing the Declaration of Expenditures".**

In 2007, within the framework of planning period from 2007–2013, **the first advance payments of 98 308 thousand euro were received.**

Table 7. **Funds claimed and received in 2007 within the framework of the European Economic Area financial instrument and Norwegian government bilateral financial instrument, EUR**

No.	Title of the project	Type of payment	Assets claimed from financial instruments, thousands EUR		Assets claimed from financial instruments, thousands EUR	
			date	sum	date	sum
1.	Project preparing fund	advance			25.07.2007	5
2.	Non-governmental organization fund	advance			25.07.2007	99
3.	Project preparing fund	transitional	18.10.2007	390	01.11.2007	390
4.	Non-governmental organization fund	transitional	18.10.2007	400	01.11.2007	400
	Total			**790**		**894**

Source: the Treasury

[6] Based on Article 31 of 21 June 1999 EU Council Regulation No.1260/1999, the European Commission automatically reduces the amount of financing available under Structural Funds by the outstanding (undisbursed) amount which has not been paid to the Structural Funds beneficiary and has been declared to the European Commission by the end of the second year following the year of committment.

4. State-funded pension scheme asset management

In 2007, the Treasury performed **its last** management of the State-funded pension scheme assets (second-tier pensions) in **accordance with the State-Funded Pensions Law**, which assigns this function to the Treasury as the government agent.

In 2007, the Treasury discontinued management of State-funded pension schemes. On 31 October 2007, **the net asset value of the Treasury investment plan was zero lats. All parts have been removed.**

When the Treasury's investment **plan was completed, the value of one part of the plan was 1.265.** What this means is that each lat invested since the beginning of operation in 2001 has induced a profit of 26.5 santims, or on average 4.4 santims per year. Taking into account that income from the investments is being reinvested, at constant profitability, the income from investments in absolute expression increases with every year. Capital invested can increase in amount several times. Consequently, **the total value of assets of the investment plan reached 10.3 million lats.**

In November 2005, the Cabinet of Ministers expressed their support of option D of the concept **"On Further Operation of the Treasury in Management of the State-Funded Pension Scheme Assets"**, providing for a transfer of the **Treasury's investment plan portfolio to private asset managers.** The Treasury prepared **adequate amendments to the State-Funded Pensions Law**, which were adopted by the Saeima on 28 September 2006.

In a tender organised by the Ministry of Finance, **rights to overtake the accrued capital of the Treasury's investment plan on the state-funded pension scheme** were obtained by all eight managers of assets, who had submitted their applications to the Ministry of Finance. **The Treasury and SSIA ensured the change of investment plan to 30 October 2007 for those participants of the Treasury's investment plan, who had not chosen a different manager of assets and investment plan until 28 September 2007.**

The investment plan of the Treasury was **conservative**, which does not foresee investments into securities of commercial institutions, other capital securities and securities equal to these. **The Treasury invested assets of the second level in Latvian government securities, mortgage bonds, deposit certificates and time deposits in Latvia's banks**, taking into account the following **restrictions**:

1) Up to 100% of the Treasury's investment plan assets may be invested in domestic government loan debt securities, but in securities of one issue – up to 20% of the total amount of assets managed by the Treasury, providing that the Treasury's investment plan assets contain domestic loan securities from six or more issues;
2) Investments in mortgage bonds and deposit certificates of one issuer may not exceed 10% of the Treasury's investment plan assets;
3) 25% of the total amount of assets may be invested in bank time deposits, but no more than 10% of assets received for managing in one bank.

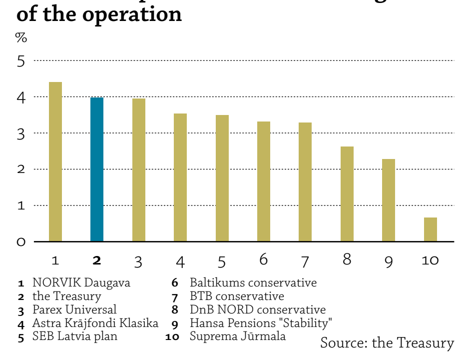
The efficiency of the Treasury's investment plan assets may be assessed by comparing its profitability to the profitability of other plans. The Treasury's investment plan has discontinued its operation and there is no opportunity to save the securities until repayment, which would improve the profitability of the plan. However, **profitability of the Treasury's investment plan since the start of operations (3.94% per year) is the second best showing among ten conservative plans.**

Concept – **The prospect of an investment plan** on the operation of the Treasury in the State-funded pension scheme approved by the Treasury on 26 July 2001. On 7 September the SSIA transferred the first assets (89.5 thousand lats) to the Treasury's investment plan account. As the Treasury was the exclusive manager of the second stage pension scheme in 2001 and 2002, the amount of assets to be managed increased sharply, and at the end of 2002 the amount of assets of investment were 12.3 million lats.

In January 2003, private managers began to operate in the management of the second stage pension scheme. Currently there are nine private managers operating in this scheme offering the participants of the scheme a choice of 25 various plans – nine conservatives, four balanced and 12 active plans.

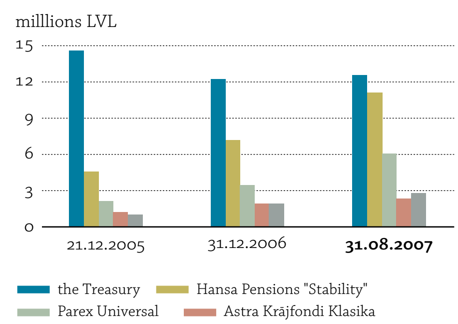
With the involvement of private managers in the second level of assets management of a pension scheme, many scheme participants changed their asset manager and competition among the managers has formed. Thus, as of 2003, the value of the Treasury's investment plan assets increased slowly, achieving its maximum (15.8 million lats) in August 2005. However, among the conservative investment plans, the Treasury's investment plan had the highest value of assets until September 2007.

Chart 15. **Profitability of conservative investment plans since commencing of the operation**



Source: the Treasury

Chart 16. **Changes in net assets of the largest conservative investment plans**



Source: the Treasury

5. Corporate governance of the Treasury as a public administration institution

5.1. The Treasury's financing and its spending

The Treasury's financing is comprised of:

1) a grant from general revenue;

2) service charges and other self-generated revenue:
  - revenue from central government loan service,
  - revenue from central government guarantee service,
  - revenue for management of the assets of the State funded pension scheme.

In 2007, the Treasury implemented the following **basic budget programmes and sub-programmes:**

1) programme "Budget execution and central government debt management":
  - sub-programme "Budget execution";
  - sub-programme "Central government debt management";

2) sub-programme "Contributions to international organisations";

3) sub-programme "Compensation to rehabilitated citizens";

4) programme "Central government budget loans and their repayments";

5) programme "Grant to local government cohesion fund".

The objective of the sub-programme "Budget execution" is execution of the central government budget within the framework set by the annual law on the state budget, focusing on efficient management of the government budget funds, identification of services required by the Treasury's clients, improvement of the quality of the services offered in line with the best international financial management practice and applying the latest technologies.

The objective of the sub-programme "Central government debt management" is effective management of the government debt and assets, ensuring the funds required for the purpose of financing the government execution and refinancing of the government debt at the lowest possible costs by hedging the financial risks and taking into account the development of the Latvian domestic capital market and the overall financial system.

The objective of the sub-programme "Contributions to international organisations" is making annual membership contributions of the Republic of Latvia to international financial organisations and payments into the capital and/or reserves of the international financial institutions, where the Republic of Latvia is a holder of capital shares, in due time and full amount, thus ensuring settlement of the undertaken commitments.

The objective of the sub-programme "Compensation to rehabilitated citizens" is to ensure disbursement of compensations to rehabilitated citizens in compliance with the laws and regulations.

The objective of the programme "Central government budget loans and their repayments" is to ensure government budget lending in compliance with respective budget appropriation, offering to project implementers the most adequate financial resources, to provide current information on the budget loan portfolio issued, to perform actions required for the process of collecting delayed payments.

The objective of the programme "Grant to local government cohesion fund" is to ensure transfer of the grant from the central government budget to the Local Government Financial Cohesion Fund in compliance with the effective laws and regulations.

In 2007, funding approved in the central government **basic budget to cover expenditure was 79 478 488 lats**, including:

Table 8. **Central government basic budget funding and its spending (summary of all the programmes, LVL)**

No.	Financial assets	In the preceding year (actual)	In the reporting year	
			Approved by the law	actual
1.	**Financial assets to cover expenditure (total):**	**71 378 205**	**79 478 488**	**79 624 054**
1.1.	Grants	70 099 221	78 360 036	78 360 036
1.2.	Service charges and other self-generated revenue	1 278 984	1 118 452	1 264 018
2.	**Expenditure (total):**	**69 559 995**	**79 478 488**	**74 512 307**
2.1.	Maintenance costs (total):	68 399 853	78 257 975	73 761 639
2.1.1.	Running costs	3 947 436	7 362 168	5 579 325
2.1.2.	Interests	53 053 767	57 017 910	54 727 836
2.1.3.	Subsidies and grants	588 784	800 000	451 824
2.1.4.	International collaboration	3 656 969	5 925 000	5 849 757
2.1.5.	Grants to local governments	7 152 897	7 152 897	7 152 897
2.2.	Expenditures for capital investments	1 160 142	1 220 513	750 668

Source: the Treasury

1) a grant from general revenue in the amount of 78 360 036 lats, which is 8 260 815 lats more than in 2006;

2) self-generated revenue from the servicing of central government loans, guarantees and management of the State funded pension scheme assets in the amount of 1 118 452 lats, which is the 38 165 lats more than in 2006.

Total allocations granted under the appropriation procedure amount to **79 478 488 lats**, which is 8 050 800 lats more than in 2006. Of the granted allocations, **74 512 307 lats** were actually spent, which is 4 952 312 lats more than in 2006 or 94% of the total allocations granted in the reporting year.

In 2007, **expenditures for capital investment decreased by 409 474 lats** over the previous reporting period as a result of changes in the schedule of implementation of the project "Implementation of the Universal Central Government Budget Planning and Execution System (SAP)".

The cash balance under the basic budget sub-programme "Budget execution" at the end of the period amounted to 564 880 lats. This amount is comprised of revenue from service charges that have been above the plan for several years.

Table 9. **Central government basic budget funding and its spending for the basic budget programme "Budget execution and government debt management" (LVL)**

No.	Financial assets	In the preceding year (actual)	In the reporting year	
			Approved by the law	actual
1.	**Financial assets to cover expenditure (total):**	**59 595 308**	**65 600 591**	**65 746 157**
1.1.	Grants	58 316 324	64 482 139	64 482 139
1.2.	Service charges and other self-generated revenue	1 278 984	1 118 452	1 264 018
2.	**Expenditure (total):**	**58 161 345**	**65 600 591**	**61 057 829**
2.1.	Maintenance costs (total):	57 001 203	64 380 078	60 307 161
2.1.1.	Running costs	3 947 436	7 362 168	5 579 325
2.1.2.	Interests	53 053 767	57 017 910	54 727 836
2.2.	Expenditures for capital investments	1 162 142	1 220 513	750 668

Source: the Treasury

Table 10. **Central government basic budget funding and its spending, basic budget sub-programme "Budget execution"(LVL)**

No.	Financial assets	In the preceding year (actual)	In the reporting year	
			Approved by the law	actual
1.	**Financial assets to cover expenditure (total):**	**5 195 308**	**6 530 591**	**6 676 157**
1.1.	Grants	3 916 324	5 412 139	5 412 139
1.2.	Service charges and other self-generated revenue	1 278 984	1 118 452	1 264 018
2.	**Expenditure (total):**	**5 009 744**	**6 530 591**	**5 845 031**
2.1.	Maintenance costs (total):	3 849 602	5 310 078	5 094 363
2.1.1.	Running costs	3 849 602	5 310 078	5 094 363
2.2.	Expenditures for capital investments	1 160 142	1 220 513	750 668

Source: the Treasury

Table 11. **Central government basic budget funding and its spending, basic budget sub-programme "Government debt management" (LVL)**

No.	Financial assets	In the preceding year (actual)	In the reporting year	
			Approved by the law	actual
1.	**Financial assets to cover expenditure (total):**	**54 400 000**	**59 070 000**	**59 070 000**
1.1.	Grants from general income	54 400 000	59 070 000	59 070 000
1.2.	Service charges and other self-generated revenue	-	-	-
1.3.	Foreign financial assistance	-	-	-
2.	**Expenditure (total):**	**53 151 601**	**59 070 000**	**55 212 798**
2.1.	Maintenance costs (total):	53 151 601	59 070 000	55 212 798
2.1.1.	Running costs	358 004	2 052 090	484 962
2.1.2.	Interests	52 793 597	57 017 910	54 727 836
2.2.	Expenditures for capital investments	-	-	-

Source: the Treasury

During the accounting period, within the framework of the basic budget sub-programme “Central government debt management” total expenditures were planned in the amount of 59 070 000 lats, while the actual expenditures were only 55 212 798 lats. Allocations granted were not spent in full, as the government budget execution performance indicators were better than planned, reducing the total necessity of loans in 2007.

Interest payments were performed within the framework of the basic budget sub-programme “Central government debt management” on government borrowing from foreign and international financial institutions in compliance with agreements concluded, outstanding government securities, coupon payments on government bonds , as well as other government debt management related payments, including payment of a charge for registration of domestic government securities and their retention and securities events service at the Latvian Central Depository, as well as their listing on the main list of Riga Stock Exchange, payments for use of financial market information systems, for legal, auditing, rating agencies and other services in relation to the central government debt management. Payments to credit institutions for servicing of accounts (including servicing of credit cards), as well as interest payments for government special budget cash balances and deposits made with the Treasury have also been performed.

The Republic of Latvia is a member of several international financial institutions and organisations. By joining them it has not only acquired certain rights but has also committed itself to making payments into their capital and reserves and annual membership contributions. Therefore, within the framework of this programme the Treasury ensures that the undertaken membership commitments are fulfilled in compliance with the payment schedules. In 2007, the Treasury ensured that membership payments were made into the following international financial institutions: EBRD, EIB, NIB, Council of Europe Development Bank, World Customs Organisation and Intra-European Organisation of Tax Administrations. All payments were made in the required amounts and within the set timeframe.

In 2007, the planned amount of total contributions was 5 925 000 lats. All planned payments to international financial organisations were made in time and in full amount, totaling 5 849 757 lats. Consequently, the key objective of the sub-programme was attained. No new measures or activities that may have an impact on implementation of the sub-programme were introduced in 2007.

In 2007, compensations to rehabilitated citizens were paid in accordance with 30 December 1997 Cabinet of Ministers Regulations No.443 “Procedure to Recover the Property or Compensate its Value to Persons who Lost it as a Result of Alienation due to Failure to Pay Increased Tax Fees or who Escaped from Political Repressions of the Communist Regime”.

Table 12. **Central government basic budget funding and its spending, basic budget sub-programme “Contributions to international organisations” (LVL)**

No.	Financial assets	In the preceding year (actual)	In the reporting year	
			Approved by the law	actual
1.	**Financial assets to cover expenditure (total):**	**3 830 000**	**5 925 000**	**5 925 000**
1.1.	Grants	3 830 000	5 925 000	5 925 000
1.2.	Service charges and other self-generated revenue	-	-	
1.3.	**Foreign financial assistance**	-	-	
2.	**Expenditure (total):**	**3 656 969**	**5 925 000**	**5 849 757**
2.1.	Maintenance costs (total):	3 656 969	5 925 000	5 849 757
2.1.1.	International collaboration	3 656 969	5 925 000	5 849 757
2.2.	Expenditures for capital investments	-	-	-

Source: the Treasury

Table 13. **Central government basic budget funding and its spending, basic budget programme “Compensations to rehabilitated citizens” (LVL)**

No.	Financial assets	In the preceding year (actual)	In the reporting year	
			Approved by the law	actual
1.	**Financial assets to cover expenditure (total):**	**800 000**	**800 000**	**800 000**
1.1.	Grants	800 000	800 000	800 000
1.2.	Service charges and other self-generated revenue		-	-
1.3.	**Foreign financial assistance**		-	-
2.	**Expenditure (total):**	**588 784**	**800 000**	**451 824**
2.1.	Maintenance costs (total):	588 784	800 000	451 824
2.1.1.	Subsidies and grants, including contributions to international organizations	588 784	800 000	451 824
2.2.	Expenditures for capital investments	-	-	-

Source: the Treasury

Table 14. **Central government basic budget funding and its spending, basic budget programme "Grant to local government financial cohesion fund" (LVL)**

No.	Financial assets	In the preceding year (actual)	In the reporting year	
			Approved by the law	actual
1.	**Financial assets to cover expenditure (total):**	**7 152 897**	**7 152 897**	**7 152 897**
1.1.	Grants	7 152 897	7 152 897	7 152 897
1.2.	Service charges and other self-generated revenue	-	-	-
1.3.	**Foreign financial assistance**	-	-	-
2.	**Expenditure (total):**	**7 152 897**	**7 152 897**	**7 152 897**
2.1.	Maintenance costs (total):	7 152 897	7 152 897	7 152 897
2.1.1.	Subsidies and grants	7 152 897	7 152 897	7 152 897
2.2.	Expenditures for capital investments	-	-	-

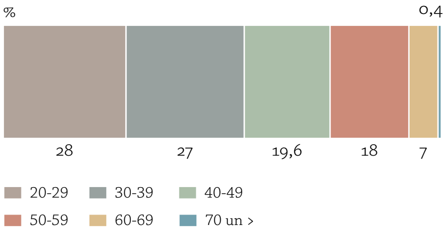
Source: the Treasury

Table 15. **Implementation of the performance indicators of the basic budget sub-programme "Budget execution"**

No.	Performance indicators	In the preceding year (actual)	In the reporting year	
			Approved by the law	actual
1.	Number of institutions	1	1	1
2.	Number of staff positions	246	301	255
3.	Treasury's expenditure per one lats of the granted central government budget allocations (LVL)	0,001	-	-
4.	Treasury's expenditure per one lats of the serviced central government debt (LVL)	0,003	-	-
5.	Timely summarised information on execution of local government and government budget and annual report on execution of the budget in compliance with term determined by Law	1	1	1
6.	Timely summarised information on execution of local government budget and prepared official monthly reports on execution of consolidated common budget	12	12	12
7.	Official monthly Treasury reports "Government debt", "external debt of the government" and "granted government guarantees" prepared	12	-	-
8.	Timely summarised information on execution of local government and government budget and prepared quarter reports	-	4	4
9.	Number of payment documents implemented by clients (in millions)	14	-	-
10.	Annual report of the foreign debt of the government and guarantees issued prepared and submitted to the World Bank	1	-	-
11.	Annual report on management of the state funded pension scheme assets under the Treasury's investment plan prepared	1	-	-
12.	Payments of the EU funding received	88	-	-
13.	Number of processed structural funds payment orders	3 293	-	-
14.	Internal quality management system documents drafted, in order to ensure the operation of the established financial management and control system for the structural funds	8	-	-
15.	Share of *eKase* payments in total amount of processed payments (%)	-	45	62
16.	Time of processing of the structural funds payment claims not longer than 20 days	-	17	12
17.	Payment of expenditures for the European Commission declared EU policy instruments for calculation of the Payment Authority (%)	-	100%	100%
18.	Ensured observation of approved government debt portfolio management showings (%)	-	100%	100%
19.	Ensured income from government budget investments in amount determined by the annual law "On the Government Budget" in the prescribed amount (actual % of the annual plan)	-	100% <	144.3%
20.	Expenditures of government debt servicing are ensured with no exceed of appropriation determined by the annual budget law (actual % of the annual plan)	-	< 100%	93,5%
21.	Central government debt at the end of the year do not exceed maximum amount determined by the annual law (actual % of the annual plan)	-	< 100%	77,3%

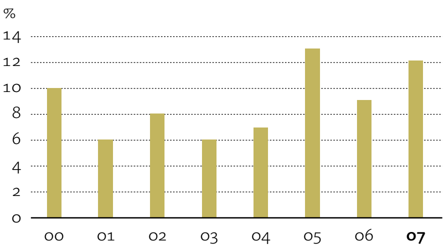
Source: the Treasury

Chart 17. **Distribution of the personnel of the Treasury by age groups in 2007**



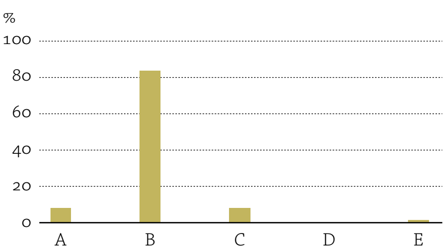
Source: the Treasury

Chart 18. **Staff turnover in the Treasury by years (2000 - 2007)**



Source: the Treasury

Chart 19. **Results of performance appraisal in 2006/2007 (%)**



A performance in all areas exceeds requirements of the respective industry
B performance in particular areas exceeds requirements; however, the remaining areas are in compliance with the requirements of the respective industry
C performance is in compliance with the requirements of the respective industry
D performance is not in accordance with the requirements of the respective industry in all areas, improvement of performance is required
E performance does not comply with the requirements in the respective industry, all areas require significant and immediate improvements

Source: the Treasury

State and local government purchases

The Treasury effected procurement in compliance with the Law "On Public Procurement" and applied procedure for an open tender, negotiations, price inquiry and procedure for procurements where the expected price of the contract is 1000–10 000 lats. For the procurement, the Treasurer establishes a procurement committee, competent in the particular area of procurement in which the contract will be signed. Procurement is registered and contracts are monitored in the Register of Procurement Contracts of the Treasury. In 2007, the total number of purchases amounted to 56 (excluding the purchases under 1000 lats), and contracts in the amount of 1 792 202 lats (VAT exclusive) were concluded.

5.2.Personnel and personnel management

The personnel are the most important resource of the Treasury, and provide achievement of the goals set by the Treasury and further development of the institution. In 2007, there were **273 positions**: in January – 241 civil servants and 32 employees, civil service or labour relations have been established with **249 civil servants and employees**. The division of the position of civil servants and employees on 28 December 2007 has changed – respectively, 245 civil servant and 28 employee positions, civil service or labour relations have been established with 253 civil servants and employees.

More than one half of the personnel of the Treasury are in the **age group of 20 to 39**: from the age group of 20 to 29–28% and from 30 to 39–27% people were employed (see Chart 17).

In comparison to 2006, the **proportion of women to men** has remained unchanged. **84%** of employees working in the Treasury are **women**, while **16%** are **men**. Only women are employed in the regional centres (except the Riga settlement centre). A similar situation may be observed among managers of structural units of the Treasury and their deputies: women – 81%, men – 19%.

In 2007, **staff turnover** in the Treasury was **12%: 30 civil servants and employees** were dismissed (staff turnover by years see in Chart 18).

Taking into account the tense situation on the labour market and the lack of professionals and demand thereof, the Treasury implements a well-considered Strategy for attracting and retaining personnel.

In the reporting year, **71 applicant selection competitions** were held for vacant staff positions at the Treasury. 32 new specialists established civil service or employment relations with the Treasury following the selection process. The Treasury continues to promote career growth for their specialists: 23 specialists of the Treasury were granted the opportunity of career development by transferring them to other staff positions as a result of staff appraisal and internal selection competitions.

In order to attract those who might take an interest in working at the Treasury and to select the most suitable candidates, the Treasury continues its cooperation with mass media, institutions of higher education and personnel recruitment and selection companies.

In order to introduce the new employees with official duties and operation of the institution, the Treasury draws particular attention to preparing of the working schedule for the new employee and presenting to the new employee functions and team of the Treasury. When the trial period is completed, performance of 35 new employees is being assessed. All the new employees have received positive assessment, which demonstrates that during the process of selection applicants having ability to apply their professional knowledge and to acquire the new duties have been selected.

Based on the appraisal results of the trial period, the State Department of Civil Service granted the status of civil servant to 21 civil servant candidates of the Treasury in 2007.

In 2007, improvement of the remuneration system of the Treasury continued both by implementing guidelines of the Treasury's remuneration system and by participating for the first year in studies on remuneration conducted by companies *Fontes Latvija* and *Hay Group*, which allow gathering of information on the labour market situation and facilitates attraction and retaining of employees.

In 2007, the **annual performance appraisal** in the Treasury was performed for the fourth time. The performances of 206 civil servants and employees were assessed (including 82 civil servants in regional settlement centres). In the appraisal of this year, an analysis of usefulness of training was also performed in order to ascertain the efficiency of training and to prepare oneself for determining further training needs. In addition, the employees' skills in orientation towards clients have been assessed in order to facilitate improvement of performance quality and involvement of the employee in achieving goals set by the Strategy.

The greatest value of the Treasury is highly educated and professional personnel. 99.2% of the staff have a university degree (including 30% who have obtained a Master's degree). Two staff members have a Doctor's degree. The tendency to develop professionally and to raise the educational level has persisted over the years (see Chart 20).

Every year the Treasury determines the need for the education of employees and approves the training plan for the following year. During the account period, 212 (84%) of public servants and employees participated in 658 training courses. In 2007, the Treasury tried to focus on adequate, specially prepared corporative trainings: in client servicing, emphasizing observation of basic principles determined in Client Service Manual, in preparation of international reports and financial reports, as well as in the area of information safety. In addition, knowledge in the area of management is being improved in trainings organized by international institutions,.

In order to ensure further development of the personnel, in 2007, performance appraisal and determination of necessity of training was improved, as well as methodology for planning and implementing of the personnel development was elaborated.

5.3.Quality and risk management

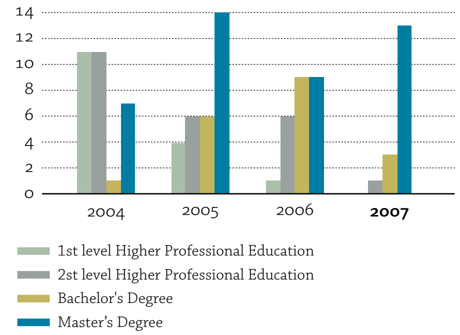
In 2007, the Treasury received a **confession letter within the framework of *Annual Efficient Management Prize 2007*** for the implementation of good management principles in a governmental institution, organised by the Confederation of Employees of Latvia in collaboration with the Chancellery, acknowledging that operation of the Treasury is in compliance with the best management principles and the Treasury is one of the most effective and best state government institutions.

In order to cut the amount of documents controlling the quality management system in less significant areas and to focus attention on the processes more exposed to risks, classification of processes by their maturity levels has been performed in the Treasury, determining the current and desirable level of maturity for each process and necessary adjustments it requires, in order to ensure necessary level of control of the process.

During the period of account, in accordance to the self-assessment of the Treasury, risks identified in the processes of the Treasury basic operation in 2008 will be attached to the **sub-processes of the basic operation classified by the level of maturity**, and risk management will be performed depending on the level of maturity of the sub-process.

In 2007, the Treasury conducted an **inquiry of clients** on the service of payment cards attached to the accounts of the Treasury, in order to improve collaboration with clients in the area of credit card services and to adjust the service, as well as to identify possible problems clients may encounter when performing functions of accounting of budget expenditures. Based on the results of the inquiry, in 2008, we plan to make improvements to the service of

Chart 20. **Education obtained by the employees of the Treasury (2004-2007)**



Source: the Treasury

credit cards attached to the accounts of the Treasury.

When assessing the Treasury management system both in the area of process management and providing services, **efficiency of internal control has increased**. The Treasury receives on a regular basis external assessment in the framework of **ISO 9001:2000 supervisory audit**, which aids in work organisation.

5.4. Internal control system

The **internal control system** of the Treasury was established, based on comprehensive basic elements of an internal control system: control environment, performance appraisal, risk management, control activities, monitoring and effective information flows and intercommunication. Internal control within the structural units of the Treasury is one of the means to prevent potential losses. In order to reduce risks inherent in administration of transactions, the Treasury implements **the double authorisation principle**, which determines that transactions have to be validated by at least two independent employees. Transacting is governed by internal quality management documents

The **results of internal audits** completed in 2007 confirmed that overall the established internal control system provides sufficient and reasonable assurance that the Treasury's assigned tasks are implemented in accordance with the strategic objectives, of performance efficiency, data correctness and reliability, compliance with legislative requirements as well as risk management and protection of the resources at the Treasury's disposal against potential losses. **The internal control system** is under continuous development: not only requirements of laws and regulations are regularly taken on board, but also best practices and experience of the financial sector.

The recommendations provided within the framework of internal audits conducted in 2007 relate to improving the budget planning and effective budget spending, improving information exchange system among structural units for planning of budget expenditures, improvements of data reserve copying process, planning of the continuity of the operation and amendments in accounting documents and procedure of accounting.

In 2007, a **self-appraisal of the Treasury's internal control system** was conducted for all the basic operation processes: execution of government budget, management of government debt and assets, implementation of the functions of EU policy instrument Payment Authority and foreign financial assistance to national fund.

5.5.Information technology development

One of the Treasury's basic priorities is the effective use of modern information systems, ensuring the discharge of the Treasury's basic functions. Therefore, in order to improve the quality of services provided, the Treasury implements continuous measures to modernise its information systems and information technology infrastructure.

In 2007, **replacement of servers** in the government budget information system and the government budget electronic settlement system *eKase* was performed, migrating them to the UNIX platform, thus ensuring compliance of performance with the increasing number of clients and transactions, the amount of which reached 14.7 million in 2007. In order to increase the safety of using the system for clients, **a unique code generator solution was implemented** for the authentication of the *eKase* and budget report system.

In 2007, work started in 2006 on a project in collaboration with the Ministry of Finance **"Implementation of a Universal Central Government Budget Planning and Execution Information System"** was continued. Within the framework of this project, a common management system of the public finances was established, which merge the functionality of the Treasury management system (government debt and asset management) and the budget execution information system, by integrating them into one system, thus preventing the shortcomings of the current systems, reducing the transaction processing time and the number of the complicated data exchange procedures. Complete implementation of the system planning block will provide an opportunity for centralised aggregation and processing of budget plans, making this process less time-consuming and using modern information technology.

In 2007, **new accounting, store and personnel management software was introduced.** This system modernises the Treasury's accounting records by ensuring fast processing of accounting information and more effective control of the process, as well as facilitates performance of functions in relation to the personnel.

In order to ensure safe and fast exchange of information on payments in euro, in 2007 **the payment systems of the Treasury were adjusted to the requirements of TARGET2**, which allows a more effective performance of payments in euros.

At the end of the year, **project of renovation and modernisation of the information technology infrastructure** of the Treasury was started, which will be continued also in 2008, when functionally and physically depreciated equipment of the Treasury's computer network communication will be changed and virtual servers will be invented, thus ensuring a base for operation of new, high-quality, fast multi-user online system.

Public Communication

Valuable communication between the Treasury and society is possible by ensuring an effective exchange of information. The Treasury informs on a regular basis mass media on issues within its competence: it prepares and distributes press releases, provides answers to questions of interest to the mass media.

One of the main priorities of the Strategy is an orientation towards clients, their needs and interests. The Treasury learns about client satisfaction by means of questionnaires.

Since 2002, the Treasury maintains its internet homepage (**www.kase.gov.lv**), where information on the institution and its functions is available. Information on the Treasury's current events is updated and adjusted on a regular basis. It is possible to ask questions as well as submit applications electronically. Visitors to the homepage can receive fast answers to their questions, whereas the Treasury has the opportunity to acquaint itself with questions of interest from their clients and, if necessary, prepare more in-depth information both on the internet webpage and for distribution in settlement centres, as well as identify potential problems and to prevent them. In order to achieve a more intensive exchange of information among the Treasury and community, in 2007, the Treasury unveiled a new version of its internet homepage, which is in compliance with the new graphical standard of the Treasury as well as the latest technologies and new content.

The Treasury's development priorities for 2008

Central government budget execution

1) In collaboration with the Ministry of Finance, elaborate a universal government finance management system (SAP), incorporating a full cycle of government budget management – from the planning of the budget to the supervision of its implementation.

2) To create reports and requests in the SAP system data stock in compliance with the structure of financing plans, government budget and on the basis of what is defined by the budget execution module of the Ministry of Finance and the Treasury unitary government budget planning and execution information systems.

3) In collaboration with partners determined by tender, elaborate technical solutions in order to ensure the opportunity to use payment cards by collecting government budget payments and charge for services provided by budget institutions.

4) To ensure unitary government and local government budget report systems and statistical report systems to the level of budget institutions.

5) To perform changes in the Treasury's government budget finance accounting policy and to prepare requests for appropriate changes in the system of the Treasury's management, in compliance with the International public sector accounting standards, national legislation and processes of finance management.

6) To continue effective use of information technologies in client services, to increase share of payments performed by eKase to 65%.

7) To improve servicing of credit cards attached to the Treasury's accounts.

8) In accordance with changing requirements of laws and regulations in the area of budget, to perform amendments to laws and regulations, defining the procedure of budget institution accounting, procedure of preparing government budget institution and local government annual reports, as well as to elaborate instructions on execution of the government budget reports.

Central government debt management

Central government debt portfolio management

1) To assess compliance of the Latvian Central Government Debt Management Strategy with the current finance market situation and to evaluate the necessity and opportunities to implement indices of the net debt portfolio indices.

2) To improve the *Cost–at-risk* model by supplementing the range of percent rate simulations with the option of multiple factor analysis.

3) To implement an option assessment model for routine use.

4) In order to make risk management of percent rates more effective, identify cash flow exposed to the percent rate risk within a particular period of time and timely limit any possible percent rate risk, as well as optimize percent payment flows to implement *GAP analysis system* for routine use.

Borrowing management

1) To elaborate the plan for attracting resources for 2009-2011.

2) In addition to the annual plan for attracting resources, assess the CP (Commercial Papers) and MTN (Medium Term Note) programmes in comparison with other similar short-term financing alternatives for government budget financing payments.

3) To improve the process of management of visits by international rating agencies.

Servicing and supervision of government guarantees

1) To elaborate the manual for business plan assessment.

2) To improve the analysis of the guarantee portfolio.

Management of assets and government budget loans

Cash management

1) To invent a *Value-at-Risk* model for routine use.

2) To invent the Delta model for routine use within the framework of the Treasury's cash management strategy and Latvian Central Government Debt Management Strategy.

3) Within the framework of asset management, ensure preparing of the fixed income securities trade portfolio in practice. To determine the parameters for optimal maintenance of the portfolio structure and to ensure trade portfolio management within the framework of *Value-at-Risk*.

Liquidity management

1) To conclude additional granted credit line (overdraft) agreements with international and local participants of financial markets in compliance with regulations provided for the Treasury by the strategic documents.

2) To assess necessary changes in methodical instructions for ensuring the Treasury's liquidity in relation to the Treasury's joining to the payment system TARGET 2.

Granting and servicing of loans

1) To participate in the elaboration of the PPP controlling normative base in the context of issues in relation to project accounting and assessing of financial risks.

2) To elaborate guidelines for granting and servicing government loans.

3) To improve the analysis of the loan portfolio.

4) To elaborate the manual for assessment of loans and business plans.

Implementation of EU policy instruments for the Payment Authority

1) To improve the process of expenditure certification within the framework of the Cohesion Fund by commencing control of mediatory institutions, in order to verify the efficiency of the expenditure declarations of the project and payment document checks.

2) In order to verify correctness, justification and compliance with regulations by EU and Member States of expenditures within the framework of the EU Structure Funds, the Treasury performs selective control of claims of project Structure Funds included in expenditure declarations, in compliance with recommendation by the European Commission auditors.

3) In order to ensure the process of spending of ES Structural Funds at the end of the planning period, perform processing and payment of submitted claims for payments from Structural funds within a shorter period of time.

Management of the Treasury as a government administration institution

1) To maintain a quality management system in accordance to the standard ISO 9001:2000 "Quality management systems. Requirements".

2) To review and simplify management of the Treasury processes and quality management system.

3) To continue the effective use of information technologies in servicing clients.

4) To elaborate a draft of proposals on possible development models of settlement centres.

5) In order to ensure further development of the personnel, improve provision of personnel in the Treasury by inventing new personality tests during the selection process of the personnel.

6) In order to ensure personnel development, improve the personnel training process by elaborating guidelines for training.

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